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**Publications of the Economic Intelligence Service
of the League of Nations.**

MONTHLY BULLETIN OF STATISTICS.
INTERNATIONAL STATISTICAL YEAR-BOOK:
REVIEW OF WORLD PRODUCTION.
REVIEW OF WORLD TRADE.
BALANCES OF PAYMENTS.
INTERNATIONAL TRADE STATISTICS.
COMMERCIAL BANKS 1913-1929.

WORLD ECONOMIC SURVEY

1931-32

PREFACE

The present Survey is the work of Mr. J. B. Condliffe, formerly Professor of Economics at Canterbury College, New Zealand, later Research Secretary of the Institute of Pacific Relations, and Professor of Economics at the University of Michigan, U.S.A.

In September 1929, the Assembly of the League of Nations, after reviewing the publications prepared by the Economic Intelligence Service in the previous year, passed a resolution requesting the Council:

“ To consider the possibility of arranging for the preparation in the near future of a comprehensive annual survey of economic developments and for the collection by the Economic Organisation of all the information required for this purpose.”

At the suggestion of the Economic Committee, to which this resolution was referred, the Council recommended to the Assembly at its next session that the proposed Survey should await the entry into force of the Statistical Convention, which aimed at extending the scope and increasing the comparability of national economic statistics. This proposal was endorsed by the Assembly, which decided, however, that the work for the Survey should be begun during 1931.

The pages that follow are the outcome of this decision. They constitute to a large extent a natural sequel to the report on “ The Course and Phases of the World Economic Depression ” prepared in 1930-31 under the direction of Professor Bertil Ohlin, of Stockholm University, and presented to the Assembly in September 1931.

While this present work by Mr. Condliffe is based mainly on data collected by the Economic Intelligence Service of the

League of Nations, the interpretation of those data is necessarily that of the author. The book is intended to afford an account of recent developments which is intelligible to the lay reader. For more detailed and technical information, the reader should refer to the publications for which the Economic Intelligence Service is directly responsible, a list of which is given on page 6.

A. LOVEDAY,

*Director of the Financial Section and
Economic Intelligence Service.*

Geneva, August 15th, 1932.

Chapter I.

A BACKGROUND OF INSTABILITY.

(i) SCOPE AND CHARACTER OF THE SURVEY.

The period during which this first *World Economic Survey* has been prepared, the year 1931 and part of 1932, has been a period of very great financial strain and economic confusion. Many of the phenomena reviewed are similar to those of a major cyclical depression ; but the length and depth of the depression, as well as its universality, suggest that, in addition to the more familiar rhythmical causes of business fluctuation, there are other and more intractable factors in the situation.

It is obvious that no survey of recent months would be complete if it did not take into account the many international consultations that have taken place and the policies evolved therefrom. In a period of crisis and derangement such as the present, concerted action, whether political or strictly economic, is of greater importance than in normal times.

The present *Survey* is, however, concerned mainly with the background of economic fact against which such action must be taken. An endeavour is made to deal, not so much with the policies of Governments or even of commercial, financial, and industrial institutions, however important, as with the confused and multitudinous activities of the peoples of the world in their everyday struggles for livelihood. Necessarily, this background of individual effort can be sketched only in broad generalities interpreted from such statistical and other information as is available. The basic structure of economic life remains decentralised and individualistic. It is true that, in addition to the Russian experiment in social planning, there has everywhere, in recent years, been a greater degree of political intervention in economic life. There has also been a strong tendency towards more definite organisation within industry itself, and towards closer integration of industry, commerce and finance. Even

allowing for these modern trends, however, the mass of economic activities still rests upon the rather confused competitive basis of effort by individuals and small groups. In this sense, there is no economic system and no hierarchy of direction or control.

Even within national units, the pattern of economic life, though it may change and may sometimes change rapidly, is largely determined by geographical resources, by population movements, by the social and cultural traditions of the people, and, strikingly in some cases, by political groupings and regroupings. There are definite limits to the possibility of adding to a country's economic stature by merely taking thought.

When international economic relations are considered, the influence of these underlying factors is even clearer. The economic world is a developing organic whole. The demands of ultimate consumers, the production organised to meet their wants, even the population and, still more, the financial resources needed in that organisation, are apt to escape national limits. The best-laid schemes either of political or of economic regulation may be baffled by shifts in demand, by the appearance of substitutes or new production, by flights from national currencies, movements of population, or changed currents of trade. Scientific and technical progress, the opening-up of new resources, colonisation of new areas, shifts of social attitudes, are always bringing new forces into play. To an economic historian of the future, the opening of the Panama Canal in 1913, the development of electrical communication, an increased awareness of the importance and possibilities of international co-operation, the penetration of scientific ideas to peoples hitherto backward, may well seem more important features of our era than many of the immediate problems that occupy our contemporary thought.

The only practical way in which these trends of worldwide economic development may be studied is by massing the complex and confused individual activities from which they emerge in statistical measurements of population change, production, trade, capital movements, shifts in the localisation of industry, changes in relative prices and similar phenomena. Not all the factors of economic change can be measured in this way, and the record of past attempts at descriptions of contemporary progress does not give much ground for expecting that the perspective of the present will correctly anticipate the proportions which future historians will ascribe to the conflicting tendencies under review. The usefulness of this *Survey*, however, does not depend upon a prophetic accuracy which experience shows to be unattainable. It is intended to register, from a contemporary standpoint, and within the limits set by available material, the actual

trends of economic development within a brief period. The emphasis throughout is upon generalised world-trends, and the aim is objective exposition rather than explanation or interpretation.

(ii) THE DISLOCATION OF THE WAR PERIOD.

The economic facts of such a critical period as the present, and the relation to them of the economic policies which have been recently followed, must necessarily be considered in the setting of the recent past.

While it would be out of place, as well as premature, in this *Survey* to attempt any considered estimate of the full effect of the war upon subsequent economic development, it is necessary to remember that the post-war generation was faced with tremendous psychological as well as material tasks of reconstruction. The economic world of 1931 differs vastly from that of 1913. The hegemony of Western Europe has been challenged, not by an orderly development, but by an abrupt transition.¹ North America is more powerful financially, a new complex of international trade is growing up in the Far East, Italy has introduced its system of corporative organisation, a new Russia poses itself as a conundrum for the rest of the world. The world as a whole hesitates between the contradictory principles of international co-operation and economic nationalism, the capital movements which are its life-blood have become confused and irregular, its former reliance upon free enterprise and competition as a regulatory principle is much weakened and, as one result of this halting between opinions, its monetary mechanism has functioned with increasing difficulty and finally broken down. It is not too much to say that the war threw the economic world off its pre-war centre of gravity, and, in doing so, liberated new forces which are not yet easy to appreciate either in regard to their power for change or in regard to the directions where they will ultimately lead. The first efforts at reconstruction traced in the remainder of this chapter were efforts to reconstruct once more a stable world system; but the forces of instability let loose by the war have proved unmanageable in the first attempt.

(iii) THE WORLD'S POPULATION.

In the post-war period there has been a marked accentuation of the movements which have for some time been tending, if

¹ Cf. Alvin H. Hansen, *Economic Stabilisation in an Unbalanced World*; New York (Harcourt Brace), 1932, Chapter I, for a discussion of the acceleration and distortion of pre-war tendencies to change.

not to redistribute the population of the world, at any rate to shift its centre of gravity. There is at present no possibility of securing complete statistical information even concerning such an elementary fact as the total number of the world's population. Such information as is available must be interpreted with very great care. In the accompanying map,¹ an endeavour has been made to put together, for rough comparison between large significant areas, two basic estimates—the total numbers of the population in 1930 and the approximate rates of increase in the decade 1920-1930. In order to emphasise the very approximate nature of the estimates made, they have been shown in round figures, millions of inhabitants, and decennial rate of increase per thousand.

There are further qualifications, however, which must be added. Not only are the total numbers of population not known in many States, but there is no possible method of indicating the character of the various populations as regards density in relation to resources, age-groupings, occupation, vitality or economic efficiency.

As for the rates of increase shown, there is obviously great difficulty of estimation in many areas. When a rough calculation is at length made, it is compounded of two factors—the natural increase of births over deaths and the loss or gain by migration. Some attention is given later to the remarkable changes in migration movements since the war; but it is not possible to estimate the separate influence of migration as distinct from natural increase in the expansion of the areas considered.

Despite the qualifications which must be attached to the calculations, they appear adequate to support certain broad deductions. Probably the most significant of these is the obvious tendency towards the stabilisation of the population of Western Europe.

The only great region which has apparently increased more slowly is China, where the figures are very uncertain. For the total population, the estimates of Chinese statisticians, as expressed, for example, in papers presented to the meeting of the International Institute of Statistics at Tokyo in 1930, have been followed rather than the lower estimates of some Western authorities.²

Of these two large areas of comparatively slow increase, Western Europe appears definitely to have reached a stage in the population cycle where further slowing down may be expected,

¹ Inserted at the end of the volume.

² Cf., e.g., the view taken by Professor Walter F. Willcox in his survey of the world's population which prefaces the second volume of *International Migrations*: New York, National Bureau of Economic Research, 1930.

because of the increasing age of the population and the declining birth-rate. The position in China is more obscure and, in the opinion of some students, there are strong factors making for increase in the future. If the spread of scientific ideas and industrial progress should continue and, at the same time, the death-rate is lowered by better control over epidemic and other diseases, the tendency to increase will be greatly strengthened.

It is perhaps significant that the areas of most rapid increase are those where the utilisation of agricultural and mineral resources has hitherto been backward. This development is clearly seen when the more detailed demographic statistics of each country are studied. British Columbia shows a high rate of increase among Canadian provinces. California has increased by almost 66 per cent in ten years, as compared with the average United States increase of 16 per cent, and the Hawaiian Islands have increased by 42 per cent. There has been a very marked increase in the Malayan region — the population of British Malaya has grown by 31 per cent, that of Sumatra by 31, of Java by 19, of Dutch Borneo by 36, of the Celebes by 36 and of the Philippines by 16 per cent. As the immigration and trade returns show, there is evidently a new economic grouping developing in the region from India to Japan. There has also been a substantial increase of population in Asiatic Russia, but it is difficult to estimate even an approximate figure for it.

There are, of course, many conflicting and contradictory tendencies. There is always in process an ebb and flow of population within national boundaries, domestic migration following economic opportunities. In Australia, the high rates of increase in Western Australia and Queensland seem to reflect immigration and protective policies which particularly affect those States. In the Argentine, an average increase of 31 per cent is by no means evenly spread over the whole country, but is most pronounced in the southern provinces. In British South Africa, the Rhodesias are growing faster than the Union. In the United States, there is rapid development all along the Pacific Coast, in the new manufacturing south and in the automobile region around the Great Lakes. In Canada, there is rapid development on the Pacific coast and new mineral activity in northern Ontario. But the variety of forces at work is perhaps best illustrated by reference to the map of Europe.¹

The first fact that leaps to the eye is the rapid increase of the peasant agricultural populations in Eastern Europe. The highest rates of increase are in Greece (27 per cent) and Bulgaria (23 per cent). In the former, the settlement of refugees after the war

¹ Inserted at the end of the volume.

added considerably to the population, and there was some refugee settlement in Bulgaria also ; but in both cases birth-rates are high. Yugoslavia (16 per cent), Poland (16 per cent) and Roumania (15 per cent) are also increasing fast in numbers. In the Baltic countries, there are considerable differences of development. Tariff policies, trade relations with Soviet Russia, the position of important pre-war ports like Memel and Danzig complicate a situation already disturbed by changing trade and varied resources.

The Scandinavian countries and Finland show conflicting tendencies also. Sweden, as a whole, increased only by 4 per cent, but the district around Stockholm increased by 19 per cent, and new mineral enterprises in the north, plus timber and agricultural development, also attracted population.

In Western Europe, one of the most marked features has been urban concentration. Berlin and Hamburg increased much faster than the rest of Germany. The region around Rome has apparently increased almost four times as fast as the average for all Italy. In Spain, too, the urban areas have increased rapidly ; but the clearest example is in Great Britain ; there has been a marked shift of industry from north to south and several counties around London have increased by from 20 to 30 per cent, though the average for Great Britain as a whole is less than 6 per cent.

Both in Britain and in France, and to some extent in Sweden and Norway, there has been rural depopulation. Every section of Ireland and practically every county in Scotland and Wales, as well as some rural districts in the east of England, show a decline of population. There is a similar decline or a small increase in a great belt of central France and in the south-west of Belgium.

In all these countries, there are distinct indications of re-grouping and re-localisation of industries, apart from the drift to urban centres. Thus in France, the heaviest increase is shown in the industrial north and in Lorraine ; there is a noticeable thickening of population on the coalfields which straddle the Dutch-Belgian border, and in England some parts of the Midlands, as well as the districts around London, are attracting population. But the clearest case is that of Spain, where not only the great industrial ports like Barcelona, but also the iron and coal districts in northern and south-central Spain are increasing in numbers very rapidly.

It is clear, therefore, that there are a great many confusing, and to some extent contradictory, forces at work. It is difficult to make valid historical comparisons ; but it seems probable that the growth of industrial Western Europe (in population at least) has definitely slackened. Within Europe itself, the main

increase of population is taking place in the eastern countries. The development of such other regions outside Europe as South America, Malaya, North America¹ and Oceania is even more marked. The play of natural forces, such as the exploitation of hitherto neglected resources, has been complicated by political interference, especially by the setting-up of tariff and immigration barriers, by the progress of urbanisation, by the increasing variety of governmental services, and by a host of similar factors. But it would seem that the rapid increase of population, so characteristic of Western Europe in the nineteenth century, has now been slowed up in that region, while increasing productivity, supplemented by improved hygiene, has created a tendency for numbers to increase in the more outlying parts, not only of Europe, but of the rest of the world. The density of the masses of population in Europe, China and India is so great that even small rates of increase will maintain their dominant positions. On the other hand, the great relative wealth, as well as the more rapid rates of increase in the North and South American countries, Australia and New Zealand, and the wealth of resources in other developing regions, such as the Malayan archipelago and Rhodesia, have already exercised considerable influence upon the world currents of trade, investment and migration. It is probable that the population movements thus summarily described are likely to continue. Their operation has been modified and checked to some extent in the recent crisis; but they must be reckoned with in any consideration of the immediate future.

(iv) THE CURRENTS OF MIGRATION.

The freer movement of peoples, which resulted from the disturbance of traditional economic organisation as the new industrial technique spread from country to country in the nineteenth century, found its most effective and dramatic expression in the great trans-Atlantic migrations of European peoples. First the untilled lands of North America, and Australia and New Zealand, and, later, the developing industries, particularly of the United States, attracted great numbers from the increasing populations of almost all European countries. The South-American States also received a considerable stream of immigrants, and, in later years and on a smaller scale, a current of migration has flowed to the newly-opened agricultural and mineral resources of Southern Africa.

This movement of the European peoples was, however, declining even before the war. The capacity of the receiving

¹ See map inserted at the end of the volume.

countries was being taxed, assistance was not granted so freely, and the immigrant found it gradually more difficult to establish himself in his adopted land. For a variety of reasons, the post-war decade has witnessed a further sharp contraction of these migratory movements. Legislative restrictions were super-imposed on economic difficulties and, in the years of depression since 1929, the migration has dwindled almost to nothing.

The most important factor in this stoppage of migration has been the increasing restriction imposed by the United States. At its peak, the immigration into that country, mainly from Europe, for some years averaged over a million. In the five years immediately preceding the war, it averaged over 700,000. That figure was almost reached again in the rush to enter before the quota regulations were imposed in 1924; but there has been a steady decrease since then up to 1931, when there was a small net emigration. While the stoppage of immigration from Europe was, until the onset of the depression in 1929, partially offset by a large seasonal, and some permanent, inflow of Mexican labourers, and there was also immigration from the Philippines, as well as unrestricted migration between Canada and the United States, the virtual exclusion of European immigrants is a major economic development. It is, perhaps, correlated with the considerable increase, previously noted, of the peasant populations of Central and Eastern Europe. The United States no longer affords an outlet for the natural increase of those peoples, who are thrust back upon their own economic resources.

Immigration into Canada has not shown the same marked tendency to decrease; it has been irregular, with sharp declines in depression years. Australia and New Zealand also, after some tendency to increased immigration in the immediate post-war years, have absorbed fewer and fewer people and, finally, have registered actual losses of population by net emigration in the present depression. There has been a marked decline of immigration also in such South-American countries as the Argentine. While there may be some recovery of immigration to these areas when the depression ends, it is unlikely to be on a scale large enough to compensate for the restrictions imposed upon entry to the United States. The virtual stoppage of trans-oceanic migration from Europe must therefore be reckoned as an outstanding fact of the post-war period.

Movements within continental areas are more difficult to estimate but probably have not been on a scale great enough to compensate for the dwindling of the trans-Atlantic migration. France stands out among the European countries as receiving the largest stream of immigrants. The exact number is very difficult

to determine, as there is a constant ebb and flow of passenger traffic across the frontiers, and it is all but impossible to determine the number of immigrants as distinct from tourists, or to decide how much of the immigration is permanent and how much seasonal. The official figures show a very heavy fluctuation, the highest net figures of immigration recorded being over 200,000 in 1923, and 175,000 in 1930, while in difficult years such as 1921, 1927 and 1931 there was net emigration.

The most significant and largest contemporary movements of migration since the war have occurred in Asia. For some years, there has been proceeding a migration from China proper to Manchuria, comparable only with that of the greatest rush to the United States. Since 1907, about 200,000 Japanese and a number of Koreans, variously estimated at from 400,000 to 1,000,000, have settled in this region, together with a community of Russians roughly estimated at 80,000. But the more significant movement has been the mass immigration of Chinese peasants which set in about 1923. A seasonal movement of labourers had long been customary from the northern provinces of China proper ; but for some years after 1923 there was a greater tendency for permanent settlement of a larger number of immigrants. Various estimates have been made of the extent of this immigration, ranging from over 400,000 in 1923 to a peak of about 1,200,000 in 1927, falling again to about 300,000 in later years. Of these numbers, an increasing proportion, which rose to about 60 per cent, remained for permanent settlement and an increasing proportion of women and children has been noted among the immigrants.

The other great current of migration in the Far East in recent years has been from South-East China and, to some extent, from India to the rapidly developing tropical regions of British Malaya, the Dutch East Indies and, less important at present, the Philippines. The net gain of the Straits Settlements by immigration in the year 1926 was almost 340,000 ; but, in this region, as elsewhere, economic depression has brought about measures of restriction by all the Governments concerned. The Federated Malay States, to which, in the past few years, large numbers of Chinese labourers have migrated, seeking work in the tin mines and on the rubber plantations, were forced, in 1931, to limit the immigration to a third of the previous monthly average, and, at the same time, to provide relief work for the unemployed and make repatriation arrangements for considerable numbers.

Even in these new areas of migration, therefore, the restrictions on freedom of movement tend to multiply, especially in years of crisis. In the older areas, this tendency is much more pro-

nounced. It is clear that such migration restrictions should be included among the many ways in which, in the post-war period, almost all Governments have interfered with the free play of economic forces.

(v) THE SPREAD OF THE INDUSTRIAL REVOLUTION.

The fact that population is increasing faster in the countries which have not hitherto been highly industrialised—in Eastern Europe as well as in the Americas and Asia—raises the question as to how far industrial development follows this shift of population.

New industries, established in regions where the large-scale organisation of industry for a considerable time has built up both markets and auxiliary aids to production, gain many advantages of economical production. The existence of a large market and of transport, banking and commercial facilities, as well as the convenience of proximity to related and subsidiary forms of production, abundant supplies of skilled labour and technical knowledge, and saving of time and interest charges give strength and resilience to already established industrial areas. Yet technical progress is always tending to undermine these established positions and such an event as a great war, followed by years of unsettlement, may well prove a turning-point in the localisation of important industries by providing the occasion to build new industrial aggregations which, in their turn, develop strength from the very fact of their size.

In the decades immediately preceding the war, and still more in the first post-war decade, the relatively more rapid rate of increase in consumer's demand in North and South America, Australia and New Zealand has provided a powerful incentive to localisation of manufacturing industries in those regions, and the same forces are observable also in Asia.

Attention has already been drawn to the fact that these are regions of rapidly expanding population.

In the post-war decade, production and national income increased rapidly in these countries also, especially in Canada and the United States, so that there is little doubt that there has, for some time, been a definite pull of rapidly increasing consumer income attracting industrial development to these regions.

A second factor which has an important bearing on the localisation of industry is the cost of transport. The cost of transport by sea has decreased substantially. For many technical reasons, as well as because of greatly increased shipbuilding just after the war, ocean freight-rates have fallen heavily.

*Index Numbers of Ocean Freight-rates and Wholesale Prices,
1913-1931.*¹

Year	United Kingdom		United States		Germany	
	Freight index	Wholesale prices	Freight index	Wholesale prices	Freight index	Wholesale prices
1913 . . .	100	100	100	100	100	100
1924 . . .	127	165	106	141	106	137
1928 . . .	110	142	97	139	102	140
1930 . . .	82	113	85	124	92	125
1931 . . .	85	98	85	105	84	111

The costs of land transport are much more difficult to estimate. There is increasing competition on the roads and in the air, both for passenger and for freight traffic. Such indices as are available, however, suggest that railway rates, while probably not, on the average, higher than before the war in relation to the general level of wholesale prices, have not fallen as much as sea freights.²

Certain conclusions emerge from these facts. Transport costs, and especially sea freights, being lower, are a less important factor in the localisation of industries, which are therefore attracted by other forces such as increasing consumer's demand.

A further consequence of the reduced costs of sea transport has been the diminished importance of coal deposits which, in the nineteenth century, were perhaps the dominating factor in the localisation of industries. Manufacturing grew up on the coalfields or at such ports as could provide cheap coal by utilising it for return cargo. Not only is it now cheaper to transport coal, but the importance of coal as a source of power constantly diminishes. There have been great technical improvements in the utilisation and economy of coal and, in addition, competitive sources of power, particularly petroleum and electricity, have been rapidly developed. The world production of coal remains at about the same level as before the war; but the production of other sources of power has increased greatly.

¹ United Kingdom, *Statist*; United States of America, U.S. Department of Commerce; U.S. Bureau of Labor Statistics; Germany, *Wirtschaft und Statistik*.

² See report of the Special Committee on Competition between Railways and Waterways (League of Nations document C.127.M.43.1929.VIII) and *United States Commerce Year-Book*, 1930, I.

*World Production of Coal, Lignite and Petroleum.*¹
(000,000's omitted.)

Year	Coal		Lignite		Petroleum	
	Metric tons	Index	Metric tons	Index	Metric tons	Index
1913 . . .	1,216	100	127	100	54	100
1924 . . .	1,192	98	169	137	141	261
1928 . . .	1,250	103	214	166	183	342
1930 . . .	1,213	100	192	149	195	365
1931 ² . . .	1,068	88	176	139	189	350

It is not surprising to find, therefore, a distinct tendency for industry to be released from its former dependence upon proximity to coal supplies so that it is freer to establish itself close to the growing consumer's demand or to sources of bulky raw materials. The statistics show that, in fact, these two attractions tend to coincide. The production of raw materials is increasing fastest in those regions where population and consumer's income are expanding.

Besides the two related factors of increasing consumer's demand and supplies of raw material, which are tending to attract industrial development away from the older centres of concentration and particularly from Europe, there must be considered the important factor of labour supply and labour cost. There is much controversy and uncertainty concerning the extent to which lower labour costs offer competitive advantages to the establishment of industries in countries with relatively low standards of living. The whole problem is greatly confused by the attention directed to the wage-levels, rather than to the costs per unit of output. When the efficiency of the labourer is considered, it is obvious that there is no necessary connection between low wage rates and low costs of production. Various investigations have shown that any advantages of lower costs of production possessed by the textile industries now developing in the Far East are very little due to low labour rates per unit of production; they are derived rather from such factors as proximity to the market, utilisation of up-to-date machinery, and better industrial organisation. It might indeed well be argued that low standards of remuneration reflecting low levels of efficiency, instead of providing an encouragement to industrial development, offer the most difficult obstacle to it.

¹ *Statistical Year-Book of the League of Nations, 1931-32.*

² Partly estimated.

A German economist has recently attempted a statistical verification and measurement of this tendency towards the dispersal of manufacturing production by endeavouring to answer the question whether the post-war industrial developments in the countries outside Europe were merely a passing effect of the war or part of a permanent tendency towards the dispersion of industry.¹ By dividing the industries of a number of countries into various types characteristic of different stages of industrial development, he was able to demonstrate a clear tendency for progression from a stage dominated by simple goods for immediate consumption, through an intermediate stage, to one where industries engaged in "real" capital production provided more than 50 per cent of the production of the country. It may therefore be inferred that the tendency towards industrial development in hitherto backward lands is likely to continue.

(vi) THE RESTORATION OF PRODUCTION.

At the conclusion of the war, there was in the world as a whole a state of general economic confusion. On the one hand, there was a widespread shortage of important foodstuffs and raw materials in those areas which had felt the effect of years of blockade. In certain instances, this impoverishment threatened actual famine, which was not easy to avert, since not only the organisation of essential services, such as transport, but also the credit and trading mechanism had largely broken down, while the spirit of the people was temporarily affected by privation and defeat. These difficulties were accentuated also by the disordered public finances and currency strains, which resulted in successive flushes of inflation that completed the destruction of public confidence. Moreover, actual hostilities dragged on in various parts of Europe for several years after the principal conflict terminated at the end of 1918.

On the other hand, the war effort in some countries, particularly in industries like shipbuilding, had just begun to reach the peak of productivity, while other forms of production less essential for war purposes had been starved of resources and labour. The sudden reversal of the powerful machinery that had been built up for the prosecution of the war, the resumption of peace-time activities, the loosening of State control and release of private enterprise, and the reabsorption into normal industry of millions of combatants presented gigantic problems of readjustment. Stocks of commodities like wool suddenly appeared

¹ W. Hoffmann, *Stadien und Typen der Industrialisierung*. Jena : G. Fischer, 1931.

as a crushing weight upon the markets ; but, as hitherto repressed demands made themselves felt, most of these stocks rapidly disappeared and world shortages were revealed. Since war-controls were, in most cases, abandoned soon after the war ended, the necessary readjustments of demand and supply involved violent fluctuations in prices which, together with the sudden cessation of war credits, were primarily responsible for the acute financial crisis of 1920-21. The turnover from the concentrated effort at providing military resources to the decentralised competitive resumption of the multifarious activities of peace not only involved the scrapping of vast quantities of specialised equipment, but created a period of confusion which was at least equally wasteful.

The restoration of the material destruction caused by the war and the further increase of productivity necessary to regain and surpass the pre-war levels of output were not, however, the most difficult tasks confronting the post-war generation. The stimulus of war effort and the breaking down of traditional restrictions left important legacies, not only of mechanical invention, but also of organisation. The really difficult problems of the first post-war decade proved to be, not the increase of material production, but the balancing of effort and resources between countries and between industries, the reconstitution of trading relations, adjustment to the considerable shifts in income distribution caused by war debts and taxation, as well as to a greatly changed pattern of international indebtedness, and the rehabilitation of the world's badly deranged currency and banking systems.

The available statistics of production, both national and international, support this conclusion. Actual production may be measured by tabulating the total world-wide quantities of the principal foodstuffs and of materials produced in important basic industries, and by combining the results in a weighted average. This method, which has been followed by the Economic Intelligence Service of the League in the *Memorandum on Production and Trade*, first prepared for the International Economic Conference in 1927, and since continued annually, gives an index derived from a representative sample of raw materials and foodstuffs. It cannot be regarded as a measurement of the total volume of world production and still less of its value, but is an indication of the trend of production of raw materials and foodstuffs.

A brief summary of the results obtained in these calculations discloses illuminating trends. In order to obtain a comparison with pre-war times, the statistics for 1925 may be considered, since this year is now generally recognised as a turning-point

in post-war development. The year 1925 was one of comparative political settlement followed by considerable progress in financial, monetary and trading relations. Production had been steadily increasing, and an exceptionally good harvest in Europe raised the indices of production very distinctly, so that the *per capita*, as well as the total, production of the world, as measured by these indices, was greater than in 1913, though not as great as it might have been if the steady pre-war increase of productivity had not been interrupted. The situation in 1925 may best be summarised briefly in tabular form.

World Production in 1925 compared with 1913.

	Percentage (about)
Increase in world population	5
Increase in production of foodstuffs	10
Increase in production of raw materials	25
Increase in <i>quantum</i> of world trade	7

At this stage, however, it is necessary to point out that the recovery of world production after the severe depression of 1920-21 up to the year 1925 was much more marked in the rest of the world than in Europe. The following table is sufficient to show that, by 1925, Europe had barely recovered its pre-war level of production, while her trade lagged behind by some 9 per cent and her exports were still some 14 per cent below the pre-war figure. The reintegration of the post-war world had hardly begun. The process of disintegration in Europe had been arrested; but such progress as had been made in restoring the pre-war rate of increasing productivity was almost wholly in the areas outside of Europe (and particularly in North America) which had been less vitally affected by the war.

Indices of Production and Trade, 1925.
(1913 = 100.)

Region	Population	Production	Quantum of trade
Europe	101	102	91
North America	119	126	139
Rest of world	106	124	126
World	105	116	107

The next five years, from 1925 till the third quarter of 1929, offer a remarkable contrast. In retrospect it is clear that this was a period of remarkable productive activity, culminating

in a considerable boom which was, however, masked at the time by the absence of many characteristic features, particularly a rising level of commodity prices, usually associated with boom conditions. Reference has already been made to the favourable political conditions which contributed to a general restoration of confidence at this time. The evacuation of the Ruhr, followed by the first approach towards a settlement of the reparation problem by the Dawes Plan, the stabilisation of inflated currencies, successive settlements of intergovernmental indebtedness, the reconstruction of the public finances of various Central and Eastern European countries, and the political *rapprochement* signalled by the agreement at Locarno and the entrance of Germany into the League were all powerful factors in improving public confidence, to which probably the good harvest of 1925 contributed materially. A fortuitous encouragement was given to industrial recovery in many European countries also by the British coal strike of 1926.

In these more favourable circumstances, the rebuilding of Europe afforded a welcome outlet for the greatly increased productive capacity of the post-war world. The statistics, not only of production, but also of trade and capital movements, show clearly that, in these five years, there was a definite acceleration of world production and trade and that the major increases took place in Europe, which recovered a great part of its relative pre-war position, while the rest of the world continued to expand steadily. The reintegration of the world economic system had begun; but readjustments were staved off temporarily by the fact that the reconstruction of Europe demanded increasing quantities of capital and capital goods. In other words, the period 1925-1929 experienced a construction boom, based upon the need for re-equipping the European countries. The extent of this boom is perhaps best indicated by the following table, which is comparable with those cited for the previous period 1913-1925:

World Production in 1929 compared with 1925.

	Percentage (about)
Increase in world population	4
Increase in production of foodstuffs	5
Increase in production of raw materials	20
Increase in <i>quantum</i> of world trade	19

The very rapid rate of increase in the world production of raw materials shown above is fully borne out by the statistics available for various manufacturing industries in these years. The production of pig-iron in the world rose by 28 per cent;

that of steel by 33 per cent. The United States recorded an increase of 87 per cent in the demand for machine tools and a 48 per cent increase in that for foundry equipment; ship-building in the world as a whole increased by 27 per cent, the production of automobiles by 29 per cent, the production of artificial silk was 132 per cent greater, and the consumption of crude rubber 43 per cent more than in 1925.

The general evidence of these figures is unmistakable and can be stated summarily. World production of foodstuffs had kept pace with population increase, but the production of raw materials and, even more, the production of finished goods had increased much more rapidly. Within this general increase, however, there were many contradictory and fluctuating factors, so that it is necessary to examine the geographical distribution of the increasing production and to compare it with the movements of international trade.

The geographical distribution of the greatly increased production between 1925 and 1929 is best shown in the table below.

Indices of Production and Trade, 1929.
(1925 = 100.)

Region	Popula- tion	Production			Quantum of trade
		A Food- stuffs	B Raw materials	A + B	
Europe	105	110	131	117	122
North America . . .	106	97	114	105	119
Rest of world . . .	103	105	119	109	112
World	104	105	120	111	119

It so happens that the year 1929 was one of poor harvests in North America, particularly in Canada, so that the production of foodstuffs in that area was considerably lower than in the previous years.¹ Even if allowance is made for this fact, it is

¹ Comparable statistics for 1928 were :

Region	Popula- tion	Production			Quantum of trade
		A Food- stuffs	B Raw materials	A + B	
Europe	104	106	119	110	117
North America . . .	104	108	106	107	115
Rest of world	102	106	116	114	110
World	103	106	112	108	115

clear that the acceleration of world production, particularly of raw materials, was very largely due to the rapid advance in Europe. There was little compensatory adjustment in the rest of the world, which continued to increase its production steadily. More detailed examination of the statistics shows that, in the five years 1925-1929, the production of coal in Europe increased by 20 per cent, of pig-iron by 38 per cent and of steel by 41 per cent, while other basic raw materials showed similar increases.

In these circumstances, it is not surprising to find that the effort to restore Europe to its pre-war position in the world's economy without compensatory readjustments in the rest of the world should have led to a considerable degree of maladjustment in the supply and demand for essential raw materials and food-stuffs. This maladjustment was not revealed until the construction boom in Europe began to fail, but by the end of 1929 there was much evidence of the accumulation of stocks and of the existence of surplus capacity of manufacturing production and irregular price movements betokening the development of large gaps between the demand and supply of basic products.

This evidence has been fully reviewed in a previous publication of the Economic Intelligence Service of the League,¹ and need not be recapitulated here. In that publication also attention was directed to the many structural changes in industry — the mechanisation of agriculture, increased production of such materials as rubber, copper and cotton, and all the changes summed up in the term "rationalisation" of industry. The whole period was one of very rapid technical and mechanical progress, accompanied by even more important progress in the organisation of industry and commerce. At the same time, the post-war world had witnessed great changes in what formerly were relatively stable demands for basic, especially food, products. This is perhaps one aspect of the rising standard of living discussed in Chapter VIII. The dilemma has arisen of demand passing from the primitive and calculable wants to a more capricious range of desires which, however, can be satisfied only by economic organisation of an elaborate and therefore relatively fixed character.

It is not possible, in any brief summary such as this introduction to a survey of events in 1931-32, to present more than hints and suggestions as to some of the more obvious causes of instability in the immediately preceding period. The task of rebuilding the world economic order, which had been shattered by an exhausting war, was not an easy one, and it is hardly

¹ *The Course and Phases of the World Economic Depression*: Geneva, published by the Secretariat of the League of Nations, 1931, especially Chapters I and II.

surprising that the first decade of reconstruction should have revealed complex and baffling problems. The rebuilding of the pre-war world would have been a difficult task ; but the actual task of constructing a new world order, in which many elements of change had to find a place, was infinitely greater. New vested interests had grown up together with new social doctrines, and a general fear of social disorder reinforced the pleas that were insistently put forward for protection of threatened groups and industries by extraordinary public measures. In the reconstruction boom, based as it was upon large extensions of credit to countries which had never before been able to borrow upon such a considerable scale, there were inevitably some elements of wasteful expenditure, a phenomenon that was by no means confined to the borrowing countries.¹ When the flow of credit dwindled suddenly in 1928 and 1929, this waste was revealed. The burden of debt incurred, largely for sound productive purposes, but partly also for expenditure that proved to be uneconomic, was then recognised to have created obligations that were extremely difficult of fulfilment. In order to discharge these obligations, a greatly expanded volume of world trade at a relatively high level of prices would have been necessary ; but international trade, even after 1925, had barely kept pace with production, and some of the major creditor countries, so far from facilitating the payment of the obligations due to them in the only practicable way — by the receipt of goods — imposed greater restrictions upon imports. Payment might have been accepted for a time in the form of securities representing a continuing export of capital ; but, in the long run, expanding exports from the debtor countries, at least sufficient to pay the growing interest and depreciation charges, was the only permanent solution.

Towards the end of 1929, therefore, an unstable position had developed in the world's financial structure. The basic causes of this instability lay far back in the disorganisation produced by the war and the burdens of debt and taxation which it bequeathed to the post-war generation. The integration of world industry, or, to use a pre-war phrase, the " territorial division of labour ", was greatly hampered by the operation of cartels, pools, tariffs, and all the paraphernalia of the new economic nationalism, while the overhead financial obligations of nations were top-heavy and, by that very fact, created extreme nervousness. The emergence of structural maladjustments as the construction boom died away would not normally have precipitated such a severe crisis as that which developed in 1929-1932 ; but the circumstances were not normal. When the credit expansion of 1925-1929 collapsed, it was

¹ See Chapter II, section (i).

seen that the fundamental disequilibria of economic organisation had been not merely postponed but aggravated. Under the pressure of heavy financial obligations, both public and private, the debtor communities endeavoured, by pressure on the credit and price structure, to increase their active balances of external payments. Selling pressure created in this way was an important factor in causing a sharp fall in prices, but it was resisted by the imposition of further restrictions upon imports into almost all countries. The impossible situation was thus created in which virtually every country endeavoured to increase its exports at the same time as it restricted its imports, so that the selling pressure necessarily became concentrated on those few countries which endeavoured to retain a free market.

The sharp downward tendency of prices thus engendered was aggravated by the disturbance of both the financial and the monetary systems of the world. As prices fell, the inevitable result was to increase the real burden of the financial obligations which were fixed in terms of the appreciating monetary units and therefore to accentuate the necessity for providing surpluses upon international account. Since, however, the restrictions upon imports imposed by some of the principal creditor countries made it impossible for them to receive payment in goods, resort was necessarily had to payment in gold. Debtor countries and those which endeavoured to retain a free market lost their gold reserves steadily and were therefore forced into further deflation. Many of them eventually were forced, by their reluctance to carry deflation further, either to abandon the gold standard or so to restrict foreign trade and foreign payments as to maintain the nominal stability of their currencies at the cost of a virtual paralysis of international dealings. As this vicious spiral developed, even those investments which were economically sound when they were made in the boom period were rendered much more doubtful, so that the waste of the boom was, at least temporarily, greatly increased. There had, in fact, been only one practical possibility of sound reconstruction in 1925. This was to facilitate the restoration of material production by extending the range and volume of international trade, providing outlets for the increased production, not only of the reconstructed regions of Europe, but also of the outlying areas that had been stimulated during the war, allowing the forces of competition in world markets to rearrange territorial specialisation, and making possible the payment of the vastly increased financial obligations which resulted from the war, and the subsequent reconstruction, by increased export of goods, particularly to the creditor countries. Only in this way might it have been possible to carry and gradually liquidate the financial legacies of the war,

as the similar legacies of the wars of 1793-1815 and 1870 were liquidated.

Such a solution, difficult enough, as historical experience had shown, was rendered impracticable by a combination of pressures and interests — the heightened sense of economic nationalism, a reinforced desire to maintain existing standards of living for important community groups, and the general fear of social instability arising from disturbance of existing organisation by renewed international competition. The world as a whole, not as a matter of general policy but rather in a succession of immediate decisions, hesitated to embark upon the bolder course of international co-operation and, in consequence, was increasingly drawn into policies of national protection and self-sufficiency, which have proved incompatible with the discharge of the heavy international financial commitments with which the world was burdened. These commitments, disturbing and depressing as they would, in any case, have been, are impossible of fulfilment in a world where international trade has shrunk so greatly in volume, and even more in value, as barriers to exchange have accumulated and prices have fallen. The alternatives now are to restore production and trade to the levels at which these financial burdens can once more be carried or, in some way, to reduce the burdens proportionately to the lower levels of interchange and prices.

(vii) THE CHANGED DISTRIBUTION OF INCOME.

In the previous sections of this chapter, evidence has been adduced in support of the statement that, in the post-war decade, the wealth and income of the world resumed a fairly steady rate of increase, but that there were many forces at work tending to encourage that increase in the newer developing countries with expanding populations and rich resources of raw materials, rather than in the older industrial areas. The period from 1925 to 1929, when production and trade were accelerated in Europe, was in apparent conflict with the general post-war tendency; but inspection of the statistics indicates that this period of reconstruction did not, as a matter of fact, bring Europe back to a position proportionate with its pre-war share of world production and trade. The weakness of the international financial position, which was revealed when the reconstruction boom slackened in 1929, has been commented upon, and particular attention has been drawn to the general fear of insecurity which prompted the various measures taken to protect existing industrial commercial and banking enterprises and community groups.

There is a very direct and important connection between the unstable position which developed in international finance and the attempts to safeguard the security of existing national organisation. As will be shown later in this chapter, the magnitude of the reorganisation necessary to meet the changed international financial situation was very great. Such reorganisation, on a more limited scale, was achieved from time to time in the pre-war economy by changes in national price-structures, generally induced by monetary causes, particularly operations affecting the short-term rates of interest. Countries with increased international obligations to meet took steps — for example, by raising the discount rate of the central banks — to curtail national expenditure, enforce reductions in the price-level and set free financial resources for external needs.

This mechanism of adjustment has, however, worked with increasing difficulty and friction in the post-war period. For its smooth operation, a certain elasticity of the economic structure is necessary. The first effects of alterations in the bank rate and similar monetary operations are felt by the speculative markets and are normally passed on thence to industrial enterprise, so that the effect of higher money rates is to cause first a profit-deflation and then a price-deflation in the country concerned. The working of competitive economic forces in the pre-war period was such as to spread the effects of such deflation to other elements of the price-system than those immediately affected — the profits of business enterprise and the wholesale prices of commodities. It was by this spreading of the necessary adjustments that the national economic structure was brought again into harmony with its external commitments. In the post-war world, however, not only were the necessary changes very large, but the elasticity of the various national price-structures was impaired and unusual obstacles were opposed to the processes of adjustment which had formerly been relied upon. The balance of international payments was greatly altered by the financial operations of the war, and also by the unusual movements of capital in the reconstruction period, while the mechanism for effecting these payments worked with greater difficulty.

The causes for this friction are to be found partly in the changed distribution of national incomes after the war. Two or three major factors may be distinguished as mainly responsible for the change — the greatly increased burden of governmental debt which, together with increased expenditure for social services, involved relatively heavier taxation; the large transference of financial resources from industrial to *rentier* groups (now composed, particularly in the United States, of large numbers

of small investors rather than of a few wealthy capitalists), which brought changes in the form of investment and particularly increased the volume of private indebtedness which was of a fixed-interest type as contrasted with the variable-interest type of industrial shares or equities; and the sustained effort to safeguard the standard of living of important groups, particularly of wage-earners, an effort in which bank policy played at least as important a part as wage regulation. To these developments, which are common to almost all countries, there should be added the similar attempts by State action in various forms — tariffs, bounties, guarantees, contingents, etc. — to protect home industries from foreign competition, attempts which have been reinforced by the industrial action of cartels and pools.

Complete statistical measurement of all these various factors is not at present possible; but certain statistical evidence can be cited in support of the thesis that their combined effect has been to introduce much greater rigidity into the various national price-structures.

The greater volume of governmental indebtedness hardly needs statistical proof. Although some of the internal debts incurred during the war were wiped off during the inflation period, the heavy borrowings for subsequent reconstruction in most of the countries concerned have again increased governmental indebtedness. Fluctuations in currency values add to the difficulty of constructing any tabular statement showing the relation of national debt to national wealth at different periods, and the methods utilised in the various estimates that are available preclude any useful comparison of one country with another.¹

In addition to the greatly increased payments for debt services, there was a general tendency to increasing public expenditure, particularly for social services.²

The second important tendency noted above — the shift of investment from industrial shares or equities to fixed-interest-bearing securities — was closely connected with certain noticeable changes in banking policy. Direct investment in particular industries, involving risk-bearing in the hope of profit, tended to be replaced by investment either in fixed-interest securities or by long-term bank deposits, where the dominant motive was less the expectation of profit than the assurance of a fixed income. Since the operation of this tendency was achieved largely through banking institutions, it was not separable from the effects of lending policies on the part of the banks themselves, and any analysis of the problem leads, therefore, to a consideration

¹ See Chapter IX.

² See Chapter VIII, section (i).

of significant changes in post-war banking policies and the part played by interest rates in the various national credit systems. Some aspects of this question may be more conveniently dealt with later, and it is sufficient perhaps at this point to note the conclusions arrived at after detailed examination of the banking statistics of the world in the recently published *Memorandum on Commercial Banks, 1913-1929*.¹

After considering in detail "the rough parallelism between the general movements of deposits and credits from shorter-term to longer-term accounts", the *Memorandum* advances various reasons for this development, among them such changes in general economic organisation as the creation of larger industrial and commercial units financed more directly by the banks, the continued existence of "frozen credits" immobilised in the depression of 1921, and the "rationalisation" of industry. But, the *Memorandum* adds, "forces far less manageable than bank policy have been at work. . . . The continuous growth of long-term deposits (and also of long-term credits) reflects in many countries a change in the attitude of the public towards investment. Owing to the rapidity of post-war industrial and general economic changes, rapid growth of a multitude of minor industries, and the losses incurred in earlier years, the public has been less willing to invest directly in industrial undertakings by the purchase of shares or lending to such undertakings in exchange for bonds; it has preferred to keep a larger proportion of its funds in liquid form".²

The public referred to, it should be stated, is now a much larger part of the population than it was before the war. A recent American study has emphasised the fact that, under the pressure of patriotic movements, "at least 20 per cent of the population became subscribers to Government bonds and hence potential investors", whereas in the one Spanish war bond issue at the close of the nineteenth century there were only 320,000 subscribers.³ Similar developments have taken place in many other countries also.

The importance of these developments, from the point of view of the present argument, lies primarily in the fact that it is more difficult for a central banking system to make the necessary adjustments in the national economy when the debt obligations of businesses are more largely in the form of bank advances. A deflation of prices which reduces industrial profits can be met by the passing of dividends and the writing-off of

¹ League of Nations, *Commercial Banks, 1913-1929*: Geneva, 1931.

² *Ibid.*, page 48.

³ James Harvey Rogers, *America weighs her Gold*: New Haven, Yale University Press, 1931, page 52.

capital when the creditors of the businesses concerned are shareholders carrying the risks of industry. But when these enterprises have contracted indebtedness to banking institutions, such a deflation results in the so-called "freezing" of bank assets and, if long continued, may tie up the whole credit mechanism of a country and impair its financial structure. If a phrase may be adapted from the London money market, the extent to which industry is "in the banks" may give the banks extensive control over industrial policies, but may also seriously embarrass them in the conduct of the credit mechanism.

A further element of rigidity to which attention has often been called is the tendency to sustain wages and purchasing power. Detailed information concerning the rates of wages, both nominal and real, is given in various publications of the International Labour Office.¹ Even when allowance is made for changing price-levels, it is clear that in practically every country the ruling wage-rates were sustained in the post-war decade at levels above those of the pre-war period.

Parallel with this general movement to maintain wage-rates, there was a considerable extension of legislation designed to improve working conditions, to limit hours of labour, provide holidays, protect the worker from industrial diseases and insure him against the burden of unemployment.

It would be impossible, without much greater statistical information and analysis, to form any judgment as to whether the higher wage-rates that have prevailed and the extended provisions for the welfare of the workers have increased labour-costs of production per unit of output. How far the cost of these improvements in welfare has been counteracted by increased efficiency is, however, a matter which is not relevant to the argument of this section.

The continued existence of a large volume of unemployment in many countries may be taken as evidence that the economic organisation of those areas had not been adjusted to the changed post-war conditions; but the maintenance of steady and relatively higher wage-rates was only one among many factors affecting those conditions. The complete absorption of this unutilised labour would probably have called for much more drastic and fundamental economic changes than simply a reduction of wage-rates. It seems obvious, for example, that the credit policies followed in many countries made possible the continuance of levels of expenditure in many directions which could not have been maintained if, in face of the vastly increased debt commitments, an effort had been made to bring the

¹ Cf. Chapter VIII.

national economies once more on to a basis of competitive equilibrium.

It is clear, on the other hand, that the virtual pegging of wage-rates, the increased public concern for social welfare, and such expenditures as have been involved in unemployment relief added a very considerable element of rigidity to the price-structure. There was evidently a double connection between the pegging of wages and the marked inertia of retail as compared with wholesale prices.¹ The stability of wages maintained purchasing power and therefore consumer's demand, so that retail prices were sustained, while, on the other hand, the slowness with which the cost of living fell reinforced the argument for maintaining wage-rates.

When such large elements of the price-structure of almost every country were fixed and controlled in these and other ways, any changes necessary in domestic price-levels were thrown on to a narrower segment of the economic organisation, and particularly on to the profits of business enterprise. The magnitude of the changes that were involved in the redistribution of capital holdings among various countries, and the various methods by which attempts were made at readjustment, are considered in the following section. In actual fact, there was little attempt, during the first post-war decade, to meet the changed conditions by drastic alterations of the national price-structures; but it is obvious that any such attempt was bound to meet with strong resistance arising from the factors outlined above. It is not possible to estimate with any precision the extent to which the burden of readjustment was thrown upon the profits of business enterprise. There is evidence, indeed, that, during most of the first post-war decade, the necessity for such readjustment was postponed by the extension of further credits to the countries most concerned, and also by the cheap money policies pursued by those countries themselves.

There was, however, a very important fluctuation in the provision of these credits, particularly those of a short-term character. Both in 1925 and in the latter half of 1928, there was a considerable shrinkage of international lending which affected the debtor countries and caused policies of domestic contraction. The withdrawal of these credits to the industrial countries, on the other hand, afforded facilities for an investment boom in both instances, the latter example being particularly marked. Credit stringency, already difficult in the debtor countries while the boom was in progress, was greatly accentuated

¹ Cf. *The Course and Phases of the World Economic Depression*, pages 170 to 172.

after its collapse. Losses of business profits, and even capital, were almost universal; but, in certain debtor countries, these losses were of such magnitude as to endanger the whole financial structure. It has been calculated, for example, that, in Austria, as much as 80 per cent of the capital invested in over 200 companies, which were in existence in 1913, had been lost by 1930, and approximately similar proportions were lost in the case of companies formed after 1913.¹ In every country, after the depression developed in 1930, there were heavy reductions of business profits,² but it has been only with the greatest difficulty and after a considerable lapse of time that such losses have been reflected in economies of governmental expenditure, the writing-down of long-term investments and lower wage-rates.

(viii) THE FLOW OF CAPITAL.

Before the war, the international economic organisation of the world called for an increasing flow of capital, almost wholly from Western Europe, and largely from Great Britain, to the developing new countries. This flow of capital was an essential part of the orderly evolution of world industry to which attention was called in an earlier section. Population was increasing rapidly in North and South America, Australia, New Zealand and South Africa, and trade was growing also with Asia. New economic activities were developing, at first mainly agricultural, but succeeded rapidly by manufacturing. Railways, roads and shipping, banking, insurance, commercial organisation, as well as the new industries themselves, called for increasing amounts of capital investment. The pace of development was not so fast as to make the necessary adjustment of Western European industries unduly difficult. In the first stages, the increasing supplies of foodstuffs and raw materials supported both an unprecedented growth of population and a much heavier concentration of manufacturing urban industry in Europe. Later, as manufacturing developed, there was a territorial division of labour in which the countries of Western Europe continued to lead the way in providing the costly products of skilled labour, while more and more they drew revenues from the interest on their investments and the provision of shipping, commercial and financial services. In this period, Western Europe became truly "the world's banker".³ Even the United

¹ O. Morgenstern, "Kapital- und Kurswertänderungen der an der Wiener Börse Notierten Österreichischen Aktiengesellschaften 1913 bis 1930", *Zeitschrift für Nationalökonomie*, January 1932.

² *The Course and Phases of the World Economic Depression*, page 174.

³ Cf. Herbert Feis, *Europe: The World's Banker, 1870-1914*. New Haven, Yale University Press, 1930.

States, which had already begun to make foreign investments, particularly in South America, remained a considerable debtor on balance.¹

Moreover, these overseas loans of the pre-war period were dominantly long-term in character. The general feeling of confidence made it possible for investors to place their money abroad for long periods. While governmental loans were not unimportant, a very large proportion of the capital was placed in private undertakings, and even in the governmental loans of pre-war days there was a distinctively economic purpose on the whole. Exceptions would be easy to cite, but, broadly, it is true that the movement of capital before the war was predominantly an economic movement for productive and constructive purposes.²

The use of short-term credits at this period was much less in volume and very different in character from that which developed after the war. For the most part, these short-term loans were used as a "compensation balance" in international relations. A country's deficit in the balance of international payments, due to seasonal or other causes, might be met by temporary loans. If the deficit proved to be of a lasting character, it was remedied by the export of gold and the consequent contraction of credit and relative lowering of the price-level within the country concerned. The short-term loans, therefore, were used mainly as a substitute for gold movements. So sensitive were the money markets that even small changes in discount rates were normally sufficient to bring these corrective forces into play. The relatively small volume of short-term credit available moved quickly by the attraction of the ruling rates of interest as between one country and another; but the tendency always was for credit resources to be directed, as far as possible, into the more productive long-term channels of investment. Though the amounts of short-term credit involved were large absolutely, they were small relatively both to the

¹ Cf. *The Course and Phases of the World Economic Depression*, pages 28 and 29; and James Harvey Rogers, *America weighs her Gold*, page 46.

² Feis, *op. cit.*, page 27, gives a table which may be summarised as follows:

The Employment of British Capital (as at December 1913) publicly invested in Other Lands.

	£ (000,000's)	Percentage of total
Loans to Dominion and Colonial Governments	675	18
Loans to Foreign Governments	297	8
Loans to Municipal Governments	152	4
Railway securities	1,531	41
Other industrial undertakings	1,108	29

He adds (page 58), apropos of the French pre-war investments, that "much more than half, perhaps as much as three-quarters, of the total French investment served a direct economic purpose".

volume of long-term credits before the war and to the amounts that have become available since the war.

A good many Western European countries shared in this pre-war export of capital ; but the dominating part, particularly in the long-term non-governmental investments, was played by Great Britain, whose overseas investments at this time have been estimated at about \$18,000 million. French foreign loans were also considerable, perhaps \$8,700 million, and Germany, which had entered the field later, had rapidly invested something like \$5,600 million. Other countries, such as Holland, Switzerland and Belgium, were also creditors on balance, but for smaller amounts. There were considerable differences in the character of the investments, particularly as between Great Britain and France, since, in the latter country, there was a relatively larger number of small investors whose preference naturally was for loans of a governmental character largely within Europe. The dominating money market, however, was London, the influence of which was particularly strong in regard both to the long-term loans for distant constructive enterprises and to the movements of short-term credits by which international balances were mainly adjusted. It was Great Britain also that displayed the greatest readiness to provide a steady flow of new capital by the reinvestment of profits, and to face the consequences of foreign investment both by accepting a growing volume of imports from the developing countries and by making the necessary readjustments in domestic economic organisation.

The financial transactions of the war period changed this situation very radically. After the war, not only were there large shifts in the sources of capital, but the manner of lending and the proportion between long- and short-term credits, the direction of the capital flow and the attitudes of the chief lending countries towards the results of their investments have proved to be very different.

Great Britain emerged from the war with large overseas investments, even though she experienced heavy losses of former holdings and the necessities of war finance had forced the relinquishment of a considerable volume of pre-war investments, particularly in North and South America, as well as the incurring of new obligations to the United States for war purposes. International lending was quickly resumed on a large scale, so that by 1929 the total volume of British investment overseas was estimated at £3,738 million¹ — a figure almost identical

¹ Sir R. Kindersley, "British Foreign Investments in 1929", *Economic Journal*, September 1931, page 382.

with the nominal value of the pre-war holdings quoted above, although less in real value if allowance is made for the higher level of prices in 1929.

There is some evidence that, even before the onset of the world economic depression, these substantial new overseas investments of capital were made with increasing difficulty. It is not easy to arrive at a definite estimate of the balance of transactions year by year ; but the following table shows the striking decline in " annual new overseas investments, not only since 1913, but also since 1927".¹ Their decline was most marked after the restoration of sterling in 1925 to its pre-war gold parity involved a substantial measure of deflation. The coal strike of the following year was an important factor in its aggravation also.

*New Capital Issues for Foreign Account less Amortisation
Payments received in Great Britain.*

	£ (000,000's)
1913	243
1927	134
1928	108
1929	47

The position of Great Britain as a creditor country was very different and, on the whole, weaker and less stable than in the pre-war period. Though the total amount of overseas investments remained substantial, it was less in real value than before the war, and its replenishment by new capital was proving to be increasingly difficult. Moreover, the provision of such new capital (for domestic as well as foreign issues) was largely dependent upon the maintenance of credit policies which did not cripple the money markets. An increasing proportion of the funds in later years was lent in the form of short-term credits, particularly to various European countries, which later were frozen in the depression, and, on the other hand, the existence of very substantial short-term foreign holdings in London made the maintenance of both domestic and foreign lending policies precariously dependent upon international influences.

The other great lending countries of pre-war Europe were seriously affected by the war. Currency inflation disturbed the money markets so seriously in the immediate post-war years

¹ Sir R. Kindersley, " British Foreign Investments in 1929 ", *Economic Journal*, September 1931, page 383. The figure for 1913 is adjusted in accordance with the index-number of wholesale prices for 1929. These estimates represent new capital issues for foreign account, less amortisation payments received — i.e., the portion of new subscriptions for foreign account which may be estimated as taken from the current income of the country.

that it is difficult to estimate capital movements with any accuracy. Such information as is available may perhaps best be summarised in the following table. There are unfortunate gaps, but the main drift of the figures is clear.

Exports of Capital from the Principal Creditor Countries.¹

	\$ (000,000's)							
	1923	1924	1925	1926	1927	1928	1929	1930
United Kingdom ²	700	380	261	-127 ³	386	569	574	112
France ⁴					503	237	-20	-252 ³
Switzerland		23	43	28				
Belgium-Luxemburg and Congo ⁵							69	
Sweden	1	10	20	33	65	18	71	26
Czechoslovakia			17	55	61	61	24	50
United States	-104 ³	590	642	173	580	1,099	206	196

The great fluctuations in British investments have already been commented on, together with the difficulty that has been experienced in recent years in providing the large sums that were actually invested in the boom period 1927-1929. The position of France was affected immediately after the war by currency depreciation, one aspect of which was a flight of capital not easily measurable but substantial. It took the form not so much of long-term investments as of holding short-term balances abroad. After the stabilisation of the franc in 1926-27, it became possible to measure the export of French capital with more accuracy. It is evident that the repatriation of French balances was proceeding on a considerable scale as early as the latter part of 1928.

Imports of Capital to the Main Debtor Countries.¹

	\$ (000,000's)						
<i>Europe</i> :	1924	1925	1926	1927	1928	1929	1930
Germany	421	857	151	1,072	1,007	553	148
Hungary	27		26	89	91	38	24
Poland	48	69	+72 ⁶	82	124	67	
Yugoslavia	—	—	8	23	27	+13 ⁶	

¹ Indirect estimates calculated on the basis of figures relating to merchandise, gold and services. Reparation receipts and payments are included with merchandise and services.

² Excluding Government capital transactions.

³ Imports of capital.

⁴ Including the French overseas territories, except Indo-China. The amortisation of inter-Allied debts is excluded.

⁵ Excluding amortisation of inter-Allied debts.

⁶ Exports of capital.

Imports of Capital to the Main Debtor Countries (continued).
\$(000,000's)

<i>Other continents:</i>	1924	1925	1926	1927	1928	1929	1930
Argentina ¹	2	2	226	122	181	4	243
Australia ²	220	110	170	257	193	166	187
Canada	107	277	173	51	164	+87 ⁴	+160 ⁴
India ⁵	71	+69 ⁴	178	120	67	36	92
Japan	226	74	128	50	80	+9 ⁴	+128 ⁴
Dutch East Indies		+187 ⁴	+45 ⁴	+57 ⁴	0	66	34
New Zealand ⁶	22	33	67	+3 ⁴	+5 ⁴	53	49
Union of South Africa	5	34	20	72	26	46	65

The most dramatic feature of the table above, however, is obviously the emergence of Germany, which, before the war, was a creditor country, as the world's greatest borrower. Several other European countries also borrowed heavily again, especially after 1925. On the other hand, the countries outside Europe, though still eager borrowers, found themselves able to command smaller amounts of capital as the demand for Europe increased after 1926.

It remains only to draw attention to the most important of all the post-war changes in this respect.— the transformation of the United States from a debtor to a very large creditor country. In 1914, the investments of foreigners in the United States exceeded American holdings abroad by approximately \$3,000 million; but, after the war, American foreign loans had created a strong balance in their country's favour. This balance was increased heavily in the post-war period, until the net figure of American long-term foreign investments was approximately \$10,000 million at the end of 1930, exclusive of war loans with an estimated value of \$7,390 million. From this total of long-term obligations there must be deducted the amount of short-term loans held in the United States in excess of American short-term loans abroad.

Payment to the United States might have been made by increased commodity exports or by the transference of gold. Gold did flow in large quantities to that country immediately after the war. Such increase of commodity trade as took place

¹ Economic years, ending September 30th.

² IX.1923 to 31.IX.1925 : '87.

³ Economic years, ending June 30th.

⁴ Exports of capital.

⁵ Economic years, beginning March 31st.

⁶ The figures for 1927 and later years refer to economic years, beginning April 1st.

was greatly hampered, on the one hand, by high tariffs and, on the other, by reluctance to adjust the national price-levels so as to stimulate exports from the debtor countries. A solution was found by the provision of American loans which temporarily bridged the gap in the balance of payments, maintained monetary incomes and price-levels in the debtor countries, and enabled the United States to retain, and even expand, its "active" export balance of commodity trade.

This solution, obviously necessary in the immediate post-war years of economic and psychological exhaustion, postponed the necessity for wholesale and drastic reorganisation of world trade and prices, but obviously widened "the gap in the balance of payments". Its continuance depended upon the ability of the debtor countries to use their borrowings productively, so that the growing interest payments might be covered by increased income, and the capacity and willingness of world markets, particularly those of the main creditor countries, to absorb the export surpluses necessary for the payment of interest. It is clear that no permanent solution was found by piling up indebtedness covering interest charges as well as new investments.

There is perhaps a distinction to be drawn in regard to these related but separate problems of the productivity of investments and the transferability of the extra production which was developed by them. The loans which have been made naturally differ considerably in productivity. Not only must each transaction be considered on its merits, but a great deal depends upon general economic conditions in the world as a whole. Loans which were regarded as sound at a certain level of prices — either because they were invested in undertakings the increased returns from which might reasonably be expected to cover interest and repayment charges, or because the needful taxation appeared adequate to secure them — presented a different appearance when the level of prices dropped heavily and international trade was reduced. There is probably room for criticism of particular lending or borrowing policies in most countries; but the greatest immediate difficulties in the depression period arose from the vulnerability of those countries which were burdened with an undue proportion of short-term obligations. The world depression seriously embarrasses all borrowers; but those whose commitments are for longer terms are in a stronger position than those who must face demands for large repayments as well as interest.

The transfer problem, on the other hand, is common to all the borrowing countries. In so far as the investments made in them were well placed, the natural consequences were increased production and the possibility of creating a surplus out of which interest and capital repayment might normally be expected to

be paid by the transference of goods to the creditor countries. The transference of such a surplus, once created, could only have taken place through the ordinary channels of commodity trade, and the necessary stimulation of exports would have required a readjustment of national price-levels, so that costs of production were relatively lower in the debtor countries. That readjustment did not take place. The inevitable consequence was that, in the years immediately preceding 1929, there were clear signs that the transfer problem would prove difficult as soon as the supply of new loans ceased.

In 1928 and 1929, as in 1925 and 1926, there was a definite dwindling of the supply of capital available to borrowing countries, primarily because of the diversion of credit resources elsewhere. In the latter period, two main factors were responsible. A strong investment boom developed in the United States, which not only drew an increasing amount of local capital into the security markets, but also attracted short-term investments from abroad. Annual figures do not show the movement clearly, and it is complicated by the repatriation of French short-term balances ; but about the middle of 1928, the volume of capital available in the United States for foreign investment began to shrink rapidly, and the year 1929 shows a total invested abroad in this way of \$272 million as against \$727 million in 1928. In the latter year also, the accumulation of short-term balances in the United States was sufficiently great, despite the continued repatriation of French balances, to convert an outward movement of \$386 million to an inward movement of \$24 million. The combined result, therefore, was that the total of long- and short-term net movements fell from \$1,099 million in 1928 to \$206 million in 1929.

This shortage of funds available in the United States for overseas investment developed at the same time as the shrinkage of British funds, which has already been commented upon. A further very strong factor tending in the same direction was the repatriation of the French short-term foreign balances, which had been built up in the earlier years of currency disorder. Up to 1927, an annual amount, estimated at approximately \$500 million, had for some years been left on deposit for short terms in various foreign centres, especially London and New York. The money markets of the world had become adjusted to this important development, which helped to create the possibility both of foreign lending and of domestic credit expansion. The repatriation of these balances, which proceeded steadily after the stabilisation of the franc, and was reinforced later by the deposit in Paris of the short-term balances of other countries, seems to have begun early in 1928 before the shrinkage of American

foreign loans. The movement of gold to France is the counterpart of the reduction of balances abroad, as the following table shows:¹

	1927	1928	1929	1930
		Francs (000,000's)		
Net import of capital	—12,855	—6,032	+503 ²	+6,429 ²
Import of gold	14	6,509	8,673	12,320

The shrinkage of overseas loans in these various ways was accompanied by a distinct industrial and investment boom in the main creditor countries, while at the same time it created credit stringency in the borrowing countries. By the middle of 1929, a very unbalanced position had been created. The borrowing countries were forced to decrease imports and increase exports. In the raw-material-producing countries there was a contraction of credit which forced extra sales and efforts to counteract lower prices by increased production. On the other hand, the credit contraction in such heavy borrowing countries as Germany forced a restriction of imports and consumption of stocks. Both tendencies contributed to a derangement of the markets and raw-material prices sagged. When the investment boom burst in the autumn of 1929, the weak position of these commodities precipitated a rapid fall in prices, and, before recovery could be achieved, the unstable financial situation in Europe caused credit and financial stringency amounting almost to panic, which froze up the sources of capital and aggravated the crisis in every direction.

(ix) INTERNATIONAL FINANCE AND ECONOMIC NATIONALISM.

If the analysis contained in the preceding sections of this chapter could be summed up in a single statement, it would be that the post-war world as a whole had failed to realise and provide for the necessities of an economic, and more particularly a financial, system that was international in its obligations and commitments. The extent of international economic development can easily be overstated. Indeed, the problems of mal-adjustment arise largely from the fact that, while some parts of the economic, and still more the financial, mechanism are thoroughly international and even cosmopolitan, other important sections of it are still organised and planned on a national basis.

The financial structure of the world has made very rapid

¹ The territory considered includes the French overseas territories, except Indo-China. The balances, which represent indirect estimates, based on figures relating to merchandise, services and gold, exclude reparation receipts as well as payments on account of inter-Allied debts.

² Net export of capital.

strides towards complete international integration. Not only is the whole world community involved in a network of financial obligations and counter-obligations, but the delicate credit machinery that has been constructed to handle these obligations and to finance a growing world trade and an increasing degree of industrial and commercial specialisation is capable, quickly and effectively, of transferring credit buoyancy or strain from one country to another. The stock markets are closely linked, the fortunes of one affecting all the rest ; banking policies have an immediate effect upon monetary ease or stringency, not only in the country immediately concerned, but indirectly in all others. The transference of short-term credits can now be arranged by telephone, but the actual transferences and their consequences take time to work themselves out, first in the monetary sphere and later in the changed conditions of commodity trade. The world has become a financial unit and, moreover, carries a complex and very heavy burden of inter-indebtedness.

But the remaining parts of the economic structure have not yet developed to this point. Even commodity trade, widespread and important as it is, and necessary as it has become to the amenities of civilised life in every country, is much more sluggish and considerably more hampered than are financial transactions. A few sentences spoken across the ocean may cause the transference of large credits from one country to another; the country from which they go finds its exchanges depressed, perhaps loses gold and tends to find its price-level falling, and an encouragement given in consequence to exporters. In the normal course of events, the balance is righted by the actual transference of goods, and possibly by a change in the price-structure of that country as compared with others. If there were no obstacles imposed to the completion of this sequence of events, there would be little danger, but, on the contrary, many advantages in the international working of the economic system.

But as a matter of fact there still remain considerable obstacles. Even the international transference of commodities is subject to restrictions which, in recent years, have markedly increased. The economic organisation of national life that lies behind these transferences is still more resistant.

In the post-war decade, and particularly in the years just before 1929, world movements of capital and world currents of trade were not harmonised. The financing of the war, and the economic changes consequent upon war and revolution, had greatly changed the pattern of international indebtedness. There were considerable changes also in the currents of world trade. The payment of heavy interest obligations by the debtor countries could have been made in three ways — by increasing their

exports of commodities, by exporting gold, or by contracting fresh loans. Their gold resources were limited, and such losses of gold reserves as occurred placed a strain on the banking systems of many countries which, in consequence, were later buttressed by fresh borrowings. Payment by commodity exports led to strong competition between the expanded agricultural, mineral and manufacturing production of many non-European, and the restored production of the European, countries. The reluctance of some important creditor countries to receive increased imports and the failure of the debtor countries to lower their costs of production set limits also to the possibility of payment by commodity exports. Recourse was therefore had to fresh loans, which postponed the necessity for drastic reorganisation of relative price-levels and the economic structure of almost all countries, debtor and creditor alike. A further extension of credit took place and, incidentally, in its latter phases, diverted capital from those parts of the world where natural resources were abundant and population and industry were growing fast to countries already highly organised and fully populated.¹

The virtual cessation, in the course of 1928 and 1929, of this unusual capital movement revealed the instability of the situation. The financial obligations which had in the first ten years after the war been largely postponed could no longer be met by fresh borrowing. They might conceivably have been met without intolerable strain if, in the meantime, the mechanism for world trade had been extended and freed from restrictions and if, also, the debtor and creditor countries alike had been prepared to allow the forces of competition to bring about a new adjustment of world industry and commerce. This, however, they were not prepared to do. The strain of adjustment was thrown on to a small unregulated segment of economic life. It proved in the event to be intolerable, the profits of business enterprise failed and the international monetary system worked with increasing friction and difficulty and finally broke down. One country after another turned desperately to shelter its own industries while, at the same time, endeavouring to extend its outward commerce. As industrial organisation based itself upon national support and protection, and international trade fell away, the magnitude of the international financial commitments became more and more out of proportion to the possibilities of payment. These developments, however, will be traced in more detail in succeeding chapters. They were revealed unmistakably

¹ Cf. Felix Somary, *Die Ursachen der Krise*: Tübingen, J. C. B. Mohr, 1932, page 12.

in an unstable price situation towards the close of 1929, accompanied by a piling-up of stocks and a falling-off of production and trade. The subsequent break in prices and the rapid disintegration of the price-structure created problems on every side, but it is possible that, even after the break in the price-level, the situation might have been relieved with nothing more than the usual liquidation of an economic crisis. A financial crisis, however, supervened, the danger signals coming, significantly enough, from countries which had been impoverished by the war and had subsequently borrowed heavily for reconstruction. This fact in itself is sufficient to indicate that behind the rapid sequence of events traced below there lay a highly unstable situation, the roots of which are to be found in the financial consequences of the war and of the first decade of post-war reconstruction.

Chapter II.

THE DEVELOPMENT OF THE CRISIS.

(i) THE DOWNWARD TURN.

The first ten years of reconstruction after the war registered many striking successes. From the depths of depression and disorganisation in 1919, when whole populations were menaced by food shortages, there was a remarkable advance to the high level of prosperity after 1925. Currencies were stabilised, international trade was resumed and production restored. For some years, particularly after 1925, it seemed as if the major problems of reconstruction had largely been solved. The years 1925 to 1929 were, on the whole, years of considerable and widespread prosperity. Prices were practically stable, production and trade developed rapidly, and many of the characteristic phenomena of an industrial and investment boom began to appear. Beneath this apparent prosperity, however, there were the many elements of instability which have already been reviewed.

The depression which has lasted from the breakdown of these boom conditions in October 1929 till the moment of writing in the middle of 1932 was caused by a reaction from the previous period of credit expansion superimposed, as it was, upon the more fundamental elements of instability outlined in the previous chapter. The length and severity of the depression indicate that there are very deep-seated causes of economic disturbance; but it is clear also that these were largely hidden until they were uncovered by the downward swing of the investment cycle. In that downward swing, as in the preceding boom, monetary and credit policies played a very important rôle. The previous chapter dealt primarily with the non-monetary factors of maladjustment in the post-war world. Before sketching the development of the crisis, however, it is necessary to draw attention also to the monetary elements in the situation.

To trace the monetary policies of the post-war decade in adequate detail would go far beyond the scope of this volume. Certain aspects of these policies may, however, be stated very briefly. As a result of the economic and financial changes wrought by the war, the United States of America became the dominant creditor country of the world. On the other hand, the countries of Western Europe, which had formerly been a great reservoir of capital, found themselves with diminished resources and impaired credit, as well as depreciated, and in some cases unstable, currencies. In payment of obligations incurred during the war, a steady flow of gold to the United States set in. Such a flow, inevitable because there was no cheaper way of settling the balances of international payments, had the double effect of draining the gold reserves of the European and other countries and of piling up large accumulations in the United States. Since the United States was the only important commercial country remaining on the gold standard, the loss of gold did not act directly in stimulating a contraction of credit and in a lowering of price-levels, until after the resumption of the gold standard by most of the important trading countries, and more especially until after the resumption by Great Britain in 1925.

In the United States itself, it was realised that the accumulation of larger reserves would make possible an expansion of credit causing prices to rise. Banking policies in the early post-war years were largely directed towards an attempt to divert the large net inflow of gold into channels where its inflationary influence would be minimised. The volume of gold reserves in a currency system is, however, only one among many factors influencing the course of prices, and it is not possible to trace with certainty the effect of a single factor in such a complicated and changing problem. There were strong forces making towards lower prices — rationalisation and technical progress, the impoverished purchasing power of important markets, strong competition on world markets, and deflationary policies in many countries. Moreover, gold reserves are merely the foundation for a pyramid of credit, and not only the amount of credit but the rapidity or "velocity" of its turnover vary considerably according to demand.

In practice, between 1921 and 1929 in the United States, about \$700 million of the increased gold reserves were used as a backing for gold certificates which displaced Federal Reserve notes of an approximately equal amount as circulating media. The gold thus used was not, however, "sterilised", since the increase of member-bank reserve deposits (daily average) amounted, between September 1921 and September 1929, to

\$706 million.¹ It was on the basis of these increased resources of the member banks that an expansion of credit took place. During the whole of this period, therefore, there existed an ample basis for credit expansion made possible by the accumulation of larger gold stocks.

These years as a whole were years of prosperity and active business in the United States, but not of rising prices. It was this unusual combination that led to the general denial of inflationary tendencies. In the years before 1925, however, the economic situation elsewhere was so disorganised that rising prices in terms of gold and general prosperity were not possible even in the most important creditor country of the world. It is not without significance that it was in the years of flagging trade, 1924 and 1927, that the Federal Reserve Banks increased the volume of credit available, most of the increase being absorbed by the security and real estate markets.

In addition to the indirect effect of conditions abroad upon the United States commodity markets, credit policies were affected more directly by international influences, and particularly by the definite efforts at central banking co-operation. In May 1927, for example, a large movement of gold from London to Paris set in, threatening the stability of sterling, which had been restored to its pre-war gold parity in 1925. Consultations between the banking authorities of the principal financial countries were held in New York and an understanding was apparently reached. A few months later, in August 1927, rediscount rates were lowered in the United States and gold flowed out to Europe. It is noteworthy that, until the later stages of the depression, as will be shown in more detail in Chapter VI, the only post-war years in which the United States lost gold on balance were 1925 and 1928, in each case following the initiation of a cheap credit policy.

By 1927 the resumption of the gold standard had progressed a long way. Great Britain and Germany were on the gold standard again and the French currency was stabilised *de facto*, although legal stabilisation did not come till 1928. By 1927 also the very considerable increase in European industry and trade described earlier² was well under way, facilitated by stabilised currencies and renewed international trade. When the Federal Reserve Banks initiated their cheap credit policy in 1927, therefore, there were few obstacles in the international situation to an expansion of credit on a large scale resulting

¹ See C. Reinold Noyes, "The Gold Inflation in the United States, 1921-1929", *American Economic Review*, June 1930.

² See Chapter I, section (vi).

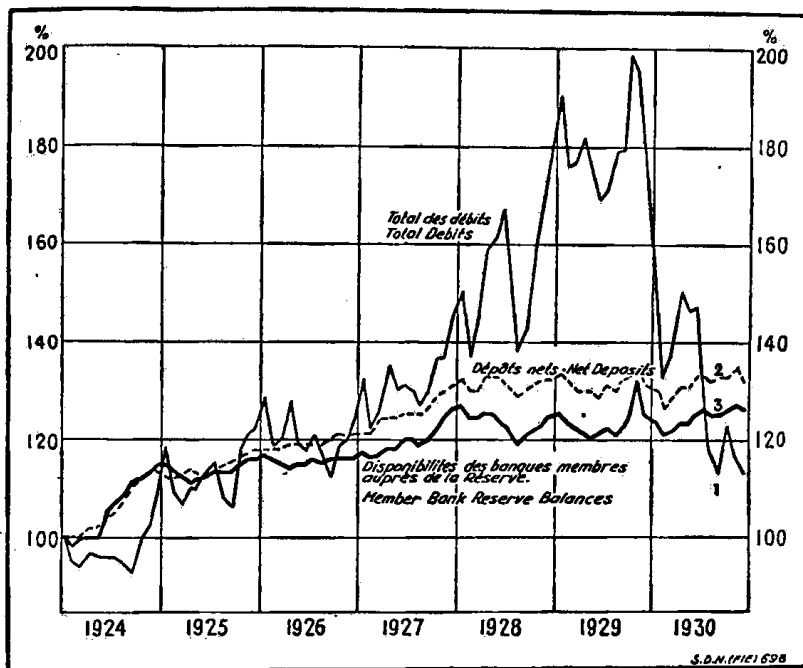
in an investment boom. The newly restored gold-standard currencies were buttressed by the outflow of gold from the United States; the reconstruction of Europe opened a wide market; international trade leaped ahead and with it the flow of capital rose to a high level.

Despite the relative stability of the indices of wholesale commodity prices, therefore, there is much evidence of widespread credit expansion after 1927. There were, indeed, many factors tending to cause lower levels of commodity prices; but it is probable that the credit expansion did in fact exert some upward influence on the price-level in the United States, which might, in the absence of such expansion, have fallen further than it did. Moreover, the stability of the wholesale commodity indices is exaggerated by the fact that they are heavily weighted with commodities entering into international trade whose prices were trending downward. The analysis of various price-movements in Chapter IV discloses definite evidence that agricultural prices particularly were sustained in the years 1927 to 1929 at relatively high levels, largely by valorisation schemes financed with cheap credit.

The expansive possibilities of the Federal Reserve system had been increased, not only by the accumulation of very large gold reserves, but also by the continued decline relatively to deposits of the holdings of vault cash by member banks. Legislation had been passed in 1917 to give greater flexibility in this respect, and investigations by the Committee on Bank Reserves of the Federal Reserve System show that great advantage was taken of the new provisions. This was especially true of the city banks, which had ready access to a Reserve Bank. The diagram on the following page shows graphically the very great expansion of credit which did in fact take place, especially after 1927. It indicates also the important fact that an enormous increase in the total volume of dollar transactions was possible without any increase in the balances maintained by member banks with the Reserve Banks. The legislation which was based upon the principle of requiring reserves of a certain proportion to the demand deposits was largely nullified, both by transfers made between time and demand deposits and by the fact that, in a speculative period, the "velocity" of the demand deposits is greatly increased.

The manner in which this very large increase in bank credit found its way into commercial and financial transactions presents some unusual features, both in the United States and internationally. There has been a general assumption that in the boom of 1927-1929, as in earlier boom periods, the expansion of credit promoted over-investment, and that this investment

*Legal Reserves, Net Deposits and Activity of Deposit Accounts
at Member Banks.¹*



1. Total debits — *i.e.*, the total dollar volume of transactions which pass through the deposit accounts of customers of member banks.

2. Net deposits — *i.e.*, member-bank time and net demand deposits combined.

3. Member-bank reserve balances — *i.e.*, reserve balances of member banks with Federal Reserve Banks.

¹ Source : "Report of the Committee on Bank Reserves of the Federal Reserve System", Washington, 1931, page 10.

for the most part went into typical production industries engaged in the production of capital goods rather than goods for immediate consumption. This assumption is supported, for example, by the Federal Reserve Board's production index, which shows, from the latter months of 1927 to the third quarter of 1929, a very considerable rise in the production of capital equipment, as contrasted with a much more modest rise in the production of consumers' goods.

The distinction between capital equipment and consumers' goods, however, is not easy to draw and a great deal depends upon the definitions adopted. Many of the staple consumption industries — textiles, leather and shoes, and food products, for example — did not share largely in the great increase of production between 1927 and 1929. On the other hand, there is a good deal of evidence that there was a considerable expansion of the newer industries catering for consumption demands. A glance at the complete list of public issues on the London money market in 1928¹ reveals the extreme difficulty of division between capital equipment and consumption industries, but the frequency of investment trust flotations, of artificial silk, gramophone, motor-car, cinema and similar issues contrasts strongly with the relative absence of overseas railways, industrial, banking or land enterprises. In the United States also, the rapid growth of production in the motor-car, radio, gramophone and similar industries suggests that a large proportion of the investment was in the industries producing goods for "durable consumption". There was, in addition, an enormous demand for new roads and road-making equipment.

There is a sense in which such production may be classified as "capital"; but much of it is consumption rather than instrumental capital, even in the case of roads, in so far as their construction has been called forth by the increasing use of cars for recreation in leisure periods. The importance of this point is increased by the fact that, in the recent boom, a considerable proportion of the production of such industries as iron and steel went to the building of cars, residential buildings and roads rather than to the building of railways or the equipment of factories in new countries.

While, therefore, it may be said that the boom was an investment boom, it is important to realise that the investment was directed largely either to the direct production of goods or services for immediate consumption, or to an increased equipment of consumption-capital, very largely of a public or

¹ *The Economic Journal*, December 1931, pages 579 *et seq.*

communal character. The boom, in other words, was directly connected with a rising standard of living. It differed somewhat from the earlier investment booms created by an excess of investments over savings, unless, indeed, the system of instalment purchases by which so much of the expansion was supported can be regarded as a form of saving. The boom was in the more durable forms of consumption goods, and the capital equipment required for their consumption and utilisation, and not in either the older and simpler articles of consumption such as food and dress, or in the heavy capital equipment of production industries, strictly defined.

There is one aspect of the investment boom which deserves further investigation. A diagram reproduced in Chapter VI indicates a distinct connection between the raising of the rediscount rates, the relative prices of raw materials and finished products and the development of industrial production. It seems probable that the increased pressure exerted by the Federal Reserve Banks in the middle of 1928 had the paradoxical result of stimulating industrial activity and speculation. This was because the higher rediscount rates affected different elements of the price-structure unequally. Prices of finished products were more resistant than those of raw materials, and as the gap between these price-groups lessened, there was some temporary stimulus to industrial production.

Moreover, a substantial proportion of the inflation in the security markets appears to have caused immediate profit-taking on a wide scale in the sense of increased consumption, mainly of durable goods, based upon the paper profits of speculation. In the international sphere also a substantial proportion of the loans which were granted in the boom period were for purposes of public consumption, such, for example, as municipal housing schemes and improvements. Indeed, it might be argued that the cheaper credit policy of the United States, by making possible similar policies in other countries, and also by providing a means of interest payments in the shape of new loans, enabled the debtor countries to maintain wage levels and standards of living that would have been impossible without such support.

The manner in which the credit expansion was largely concentrated in the security markets, particularly in the United States, is in itself significant. The following table, showing the different varieties of capital issues in the United States, shows how great was the increase in 1928 and 1929.

*Corporate Issues (New Capital and Refunding) in the United States, 1919 to 1930.*¹

\$ (000,000's).

Year	Total	Long-term bonds	Short-term bonds	Stocks
1919	2,740	634	540	1,566
1920	2,966	1,234	661	1,071
1921	2,391	1,896	215	279
1922	3,073	2,304	145	624
1923	3,232	2,316	181	736
1924	3,839	2,569	403	866
1925	4,738	3,040	387	1,311
1926	5,300	3,648	334	1,318
1927	7,319	5,190	356	1,773
1928	7,818	3,917	274	3,627
1929	10,026	2,842	263	6,921
1930	5,473	3,248	657	1,568

Such an increase is usual in periods of speculative activity. The process is simple. When abundant supplies of cheap credit are available for investment, the first effect is to raise the prices of existing stocks. An index of 90 representative stocks on the New York market compiled for the first week of September in successive years is given below.²

Date	Index of value 1926 = 100	Percentage increase in value over preceding year	Annual average yield per cent
1926	106.2		4.84
1927	131.8	24.1	4.51
1928	167.5	27.1	3.79
1929	246.3	47.0	2.94

When capital appreciation takes place so rapidly, new resources are attracted to the investment market, despite the low yields of existing stocks.

There was, however, a significant development in the new issues floated in the United States during 1928 and 1929. In the former year, 12 per cent of all new issues were supplied by new issues of shares in investment trusts. In the first six

¹ Source: *Commercial and Financial Chronicle*; summarised in the "Statistical Abstract of the United States, 1931", page 317.

² Source: *Standard Statistical Bulletin*, Base Book, 1930.

months of 1929 this percentage rose to 41, and in August of that year to 87. The total capital invested in such institutions rose rapidly, as the following table will show :

*Capitalisation of American Investment Trusts, 1923 to 1929.*¹

Year	Total capitalisation	New capital issues
	\$ (000,000's)	
1923	15	—
1924	75	60
1925	150	75
1926	300	150
1927	700	400
1928	1,575	875
1929	3,990	2,415

Much of the new subscriptions, it is clear, took the form of issues by investment trusts. The new stock issues in 1928 were \$3,627 million, and in that year investment trusts accounted for \$875 million, or almost 25 per cent. A substantial proportion of the total new investment therefore was directed to the purchase of existing securities. Moreover, a considerable proportion of the capital appreciation in the securities which were purchased was distributed in the form of dividends and thereby went to increase the already large volume of consumption.

In much the same way, the increase of brokers' loans, which was dangerously rapid in the boom, facilitated the process by which the capital reaching the investment market was transferred to consumption. Brokers' loans in New York outstanding at the end of September in successive years showed the following increases :

Year	\$ (000,000's) ²
1926	3,219
1927	3,915
1928	5,514
1929	8,549
1930	3,481

The credit available for this purpose was provided in part by the accumulation of short-term balances on the New York market on account of foreign holders, and the encashment and withdrawal of these balances was one of the causes for the collapse of the boom. As the investing public was able to obtain this increased volume of loans on the basis of the appreciated

¹ Sources : J. T. Fowler, " American Investment Trusts, New York, 1928 ", page 6, completed for 1928 and 1929 by E. Petersen in " Investment truster Statsøkonomisk Tidsskrift ", Oslo, 1931, No. 4-5, page 125.

² Source : " Statistical Abstract of the United States, 1931 ", page 319.

security values, not only was there a further stimulus to appreciation, but substantial amounts were liberated to support the increased levels of consumption.

There has been some controversy as to how far the increased speculative activity in the security markets diverted resources from the more usual channels of long-term investment. There would not appear to be any doubt as to the increasing difficulty of financing long-term industrial enterprises, both domestic and foreign, in the later stages of the boom. There was a large movement of short-term balances from other centres to New York, attracted by the high rates of interest ruling there. Foreign capital issues on the New York market show a distinct decline in 1928 and again in 1929.

*Capital Issues on the New York Market, 1924-1931.*¹
\$ (000,000's).

Year	Domestic	Foreign	Total	Percentage of total	
				Domestic	Foreign
1924.	4,588	1,005	5,593	82.0	18.0
1925.	5,125	1,095	6,220	82.4	17.6
1926.	5,189	1,156	6,345	81.8	18.2
1927.	6,219	1,573	7,792	79.8	20.2
1928.	6,789	1,325	8,114	83.7	16.3
1929.	9,420	763	10,183	92.5	7.5
1930.	6,004	1,020	7,024	85.5	14.5
1931.	2,854	255	3,109	91.8	8.2

These figures may be compared with the table quoted earlier² showing the increasing difficulty with which the London money market found new capital for overseas issues in 1928 and 1929. Investigation of the international movements of capital as disclosed by the balances on account of goods, services and gold reveals a sharp decline in the net capital exports from the United States and France in the year 1929.³ The only available figures in this connection are computed annually, but there is much evidence to show that the decline of capital available for foreign investments on these markets set in during the latter half of 1928.

This important phenomenon, which is paralleled by a diversion of capital from the domestic long-term markets, is explained

¹ Source : *The Commercial and Financial Chronicle*.

² Chapter I, section (viii).

³ See Chapter VI.

partly by the unwise flotation of numerous unsound enterprises and partly by the rising level of consumption which has already been mentioned. The extent of unsound financing in the boom may perhaps be inferred from a calculation of the values in 1931 of new enterprises floated in 1928 on the London money market. The net capital depreciation at May 1st, 1931, of the 284 new issues of 1928 was 42 per cent¹; 111 companies, with a total capital of over £25 million, had lost all their capital.²

It is difficult to set a precise date as marking the downward turn of the cycle. From the foregoing paragraphs it will be evident that, even while the investment boom was still proceeding merrily, there were many signs of difficulty and maladjustment, particularly in the debtor countries. It is probable that investment had outrun savings at least as early as 1928, and the maintenance of high levels of consumption deprived not only the debtor countries, but also many industries in the creditor countries, of the resources necessary for their development or for the maintenance of existing standards of living. It was in the debtor countries which had, wisely or unwisely, come to depend upon a steady inflow of new capital that the first signs of depression began to appear in the second half of 1928. Such international maladjustments, added to the uneasy commodity-price situation, gave warning of a dangerous instability. It was not until the investment and industrial boom broke in the autumn of 1929 that there was any very general realisation of these dangers, and it is usual therefore to date the beginning of the crisis from the collapse of the American security market in October 1929. But production in many countries was falling off before this date and commodity prices in the world as a whole began to fall in the latter part of 1928.

Reference has already been made to the accumulation of balances held by French bankers and traders in foreign centres, and further attention will be drawn to the importance of these large holdings when the movement of repatriation began after the *de facto* stabilisation of the franc in 1926-27.³ The balances were accumulated mainly in the years 1923 to 1926, partly as a result of a "flight from the franc" in the period of currency inflation and of foreign speculation in French currency. In addition, there was, during the period of currency instability, a very general practice of holding balances due to French traders in foreign currencies. For several years the French balance of commodity trade had been active, first because of the premium on exports as the currency depreciated, and later because the franc was stabilised at a low rate of exchange.

¹ If the Ford Motor Company flotation is excluded, the percentage becomes 47.

² *The Economic Journal*, December 1931, page 577 *et seq.*

³ See Chapter I, section (*viii*), and Chapter VI.

It is estimated, therefore, that after 1923 roughly \$500 million annually was added to French balances abroad. The provision of such large sums, which were used almost wholly in the short-term market, was a material factor in the encouragement of the investment boom and also in the raising of foreign loans. When these balances began to be encashed and drawn back to France in the form of gold, three important consequences followed: it became more difficult, and ultimately impossible, to maintain the security boom, foreign loans were raised with increasing difficulty both in New York and in London, and, on the other hand, the building up both of gold reserves and of credit resources in Paris promoted a considerable investment boom in France which was prolonged until well into 1930. There appears to have been some tendency for the balances to move back to France as early as the latter part of 1927; but they continued, on the whole, to accumulate till a few months before legal stabilisation in 1928. In the latter part of 1928 there was no longer any doubt of the substantial movement, and this continued at least till the end of 1931.

The movement of balances was reflected in a continuous import of gold, which swelled the reserves of the French banks. There was a steady rise of the note circulation, together with a large increase in capital flotations and savings deposits and some indication of the hoarding of currency which, after the crisis developed, increased very considerably. The capital issues, excluding those of the large railway companies, rose rapidly after the stabilisation of the franc and production also increased substantially, as the following table shows. From the middle of 1928, part of the increase in capital issues was due to conversion of old securities into new; part to fresh subscriptions.

Currency, Capital Issues and Production in France, 1925-1931.

Year	Gold reserves	Notes in circulation	Capital issues	Index of production 1913 = 100
	Francs (000,000's)			
1925	18	50	307	85
1926	18	52	401	99
1927	18	56	616	87
1928	32	62	876	100
1929	42	69	1,259	109
1930	54	76	1,823	110
1931	69	86	1,362	98

This table affords clear evidence that the investment boom in France continued long after the breakdown of the Stock Exchange speculation in the United States. The monthly index of production remained at a relatively high level until the middle of 1931.

These developments have been traced in the United States and France because these were the two great creditor countries which were able to command the largest capital resources. The other great creditor country, Great Britain, was struggling on the economic defensive throughout all the period after 1925, when its currency was stabilised at a high level. Even so, there was a marked increase in production in 1929, when the index showed a gain of 6 per cent over the previous year. In the same year the Swedish index rose 13 per cent, and remained at this high level during most of 1930. Canadian production increased 12 per cent, United States 7 per cent, and France 9 per cent in 1929.

There was, in fact, a marked increase of production in most of the great manufacturing countries, which benefited considerably from the lower prices of raw materials relatively to finished products. How far this was due to the difficulties in which the raw-material-producing countries were placed by the tendency for their imports of capital to decline, is a problem that needs further investigation. Indeed, the whole problem of the relation between the divergent movements of the prices of raw materials and finished products, the effect upon them of alterations in monetary policy, and the international implications of these relations as affecting both commodity trade and capital movements, would seem to lie at the root of the crisis.

It is at least clear that by the middle of 1929, while the investment boom was still in full swing, many of the raw-material-producing countries were experiencing financial stringency. This is true also of the great borrowing countries in Europe, which found the supply of capital available for long-term investment failing and endeavoured to meet their needs by more expensive and insecure short-term advances. In many cases they had over-borrowed, and further borrowing might merely have postponed (and aggravated) their difficulties. The weakness of their position was such that, when the break came in the New York stock market in October 1929, many forces were set in motion which combined to precipitate a severe fall in commodity as well as security markets. Severe industrial contraction reduced the demand for raw materials at the same time as the producing countries strove to liberate export surpluses, a strong demand set in for short-term credits to tide over immediate payments, and money rates were raised hurriedly, further contracting the

supply of available credit. Many of the controls by which the prices of important commodities had been maintained were weakened and further reductions of prices were inevitable.

The immediate causes of the breakdown of the Stock Exchange boom are, as always, somewhat obscure. The Federal Reserve Board, after its effort to stimulate credit expansion between August 1927 and February 1928, raised its rediscount rate and sold securities steadily in an effort to control the boom. The rediscount rate rose from 3½ per cent in January 1928 to 5 per cent in July 1928, but remained at that figure till August 8th, 1929, when it was again raised to 6 per cent. This pressure affected different parts of the price structure unevenly. The advance in the stock market was at first little affected, because higher interest rates weighed little against the prospects of capital appreciation. In the commodity markets, there appears to have developed a much earlier pressure on raw material and agricultural prices, which were tending to fall from the middle of 1928. The rediscount rate remained unchanged from July 1928 to August 1929, and during that time the very large consumption boom developed which supported prices, particularly of manufactured consumption goods, while valorisation schemes supported agricultural prices. The cumulative effect of higher discount rates, however, supported by the transference of the French balances, must have undermined the confidence of professional operators.

In the United States, the peak of production was reached in the summer of 1929 and production was falling off for some months before the break occurred in the security markets. Speculative activity on the Stock Exchange continued to increase until October, supported by such new credit devices as the investment trusts. It was not until the Federal Reserve Board began to discriminate against further advances to support security prices that this speculative activity came to an end.

The final break in such a situation is largely dependent upon more or less accidental factors of a psychological character. But behind them lies the significant fact that the speculative investment and the industrial development which it promoted, particularly in the consumption industries, finally outran consumer income. It became evident that security prices had reached levels at which the highest dividends that could reasonably be expected represented a very low yield, and it needed only a slight shock to confidence for the whole structure of inflated values to crumble. At the same time, the actual income of substantial sections of the community, such as the agriculturists, was affected when the tendency to falling prices reasserted itself.

The international side of this story is clear. The export of

American capital had created additional purchasing power in foreign markets and made possible a large active balance of export from the United States. The reduction of these overseas loans in 1928-29 came at the same time as the British money market was finding difficulty in furnishing new money, and French capital was returning in large volume to France. Gold began to flow, not only to France, but to the United States, in the early part of 1929. The result of these factors and their influence on banking policies elsewhere was "a severe crimp in credit in almost every nation all round the world". The consumers everywhere found their income inadequate to purchase the greatly increased volume of production.

There came a check, therefore, both to new capital construction and to the operations of existing plant. Unemployment increased, and "early in 1929 it became evident that the profits of American business corporations would not continue to increase. It later became evident that the profits of these enterprises would not justify the inflated prices of their securities on the stock exchange. The Federal Reserve Board began to oppose further use of bank credit to support the inflated prices of securities. The stock market tumbled, and business started on its long slide downward."¹

(ii) THE DEEPENING OF THE ECONOMIC DEPRESSION, OCTOBER 1929 TO MAY 1931.

After the break on the New York Stock Exchange in October 1929, a rapid fall of prices set in, which strengthened the already existing depression in the raw-material-producing debtor countries and gravely aggravated the already declining productivity in most industrial countries also. A detailed account of the spread of the crisis in this first period has been given in a former publication and need only be summarised here.²

The year 1930 in the United States has been described as a period of "continuous but orderly deflation in security prices, commodity prices, credit outstanding, and in the manufacture, distribution and sale of goods".³ This description is fairly typical of the generally optimistic view taken in most countries in early 1931. A year earlier, it was only from the weaker debtor

¹ See discussion, "The Business Depression of 1930", at the annual meeting of the American Economic Association, reported in the *American Economic Review*, Supplement, March 1931, pages 172-201.

² See *The Course and Phases of the World Economic Depression*, Geneva, 1931, Chapters V and VI.

³ "Commercial History and Review of 1930", *The Economist*, February 14th, 1931.

countries that reports came of discouraging conditions in 1929. Though the Stock Exchange break in October had unsettled not only security prices, but money rates and some commodity prices also, the full extent of the depression was not generally realised. There was indeed, at the end of 1929 and in the early months of 1930, some measure of relief, particularly to the European money markets. Short-term balances were no longer attracted to New York by the high rates of interest that had ruled during the boom; there was some tendency towards a reversal of capital movements back from the United States once more, the United States exported gold, and credit conditions were noticeably easier. Moreover, the advance in security prices had not reached the same proportions and had been checked earlier in most of the other principal centres, so that the shock to other stock exchanges, despite the collapse of certain speculative enterprises, was not as severe as might have been expected. When, in the spring of 1930, there was a fairly considerable rebound of security prices in New York, optimism was expressed in many quarters and there were hopes that the depression would be of comparatively short duration. The subsequent steady deepening of the depression belied these hopes, and the second half of 1930 and the first months of 1931 proved to be a period of unrelieved deflation and deepening depression. Even then, as the quotation above will indicate, the deflation was regarded in many quarters as the inevitable and wholesome liquidation period of a major economic cycle. When, however, an acute financial crisis was superimposed upon this liquidation in the early summer of 1931, the underlying gravity of the situation could no longer be ignored.

The dominant factor in the deepening economic depression of 1930-31 was the collapse of agricultural and raw-material prices. The prices of finished manufactured products were relatively well sustained; but there was a precipitate decline not only of foodstuffs, such as wheat and coffee, but also of many important minerals such as copper. For a time, animal products were less affected than the cereals, and it was noticeable that the countries where animal products were important remained relatively prosperous till towards the end of the year 1930. In the case of such countries as Denmark, Ireland, Estonia and Latvia, the maintenance of butter and meat prices, combined with a fall in cereals, gave a relative advantage in producing costs.

The following table, reproduced from the League's *Review of World Trade, 1930*, is sufficient to illustrate the range of these disparities in price movements :

Percentage Change in Average Gold Export Prices from 1929 to 1930.

1. Coffee (Brazil)	— 43	14. Petrol (U.S.A.)	— 11
2. Rubber (British Malaya)	— 42	15. Frozen meat (Argentine)	— 9
3. Wool (Australia)	— 40	16. Silk tissues (France)	— 9
4. Maize (Argentina)	— 40	17. Wood pulp (Sweden)	— 8
5. Raw silk (Japan)	— 30	18. Motor-cars up to \$1,000 (U.S.A.)	— 2
6. Tin (British Malaya)	— 28	19. News-print paper (Sweden)	— 1
7. Cotton (U.S.A.)	— 25	20. Steel girders (Belgium)	— 1
8. Copper (U.S.A.)	— 25	21. Pig-iron (U.K.)	+ 3
9. Wheat (Australia)	— 22	22. Coal (U.K.)	+ 3
10. Sugar (Czechoslovakia)	— 20		
11. Butter (Denmark)	— 19		
12. Bacon (Denmark)	— 15		
13. White cotton piece-goods (U.K.)	— 11		

These, it should be emphasised, are annual average calculations. If the percentage declines from the peak to lowest levels were taken, the fall would be heavier and the discrepancies greater.

This wholesale decline in agricultural and mineral prices in 1930 is treated in more detail later.¹ It was caused by two main factors operating in the more rigid economic system of the post-war period.² During the boom period, many, if not most, of these commodities were maintained at relatively high price-levels and production was extended behind the shelter of control or valorisation schemes financed at increasing cost. It has already been argued that the progressive tightening of interest rates in the later stages of the boom had made the maintenance of these controls increasingly difficult. Production had been extended, stocks were piling up and prices were already tending to fall, when higher interest rates followed by the collapse of the security boom swept the credit basis from under the control schemes.

The second main factor in depressing the prices of raw materials and foodstuffs is the dwindling of capital export already noted. From the latter half of 1928, the total supply of capital available in the main creditor country, the United States, fell off steadily. The debtor countries were thereby

¹ See Chapter IV.

² See Chapter I and Chapter VIII.

seriously embarrassed in the settlement of their international balances. They had come to rely upon large annual borrowings as a means of "bridging the gap" between their income and outgo. It has been estimated that the annual volume of new credits necessary for this purpose reached a total of \$2,000 million.¹ In 1928 the total of foreign investment exceeded this figure; but in subsequent years it dwindled away very considerably. There may be ground for criticism of a large part of the competitive lending which characterised the boom period, and it is probable that there must be a considerable scaling down of obligations.² Even so, the sudden cessation of lending must be recognised as a major factor both in the collapse of the price-control schemes and in the general worsening of the international financial situation in the debtor countries.

These two aspects of the problem are, indeed, inseparably intertwined. The fall in the prices of agricultural products reduced the incomes of the debtor countries and enormously increased the real burden of their debts. The pressure of their obligations in turn necessitated both heavy taxation and banking policies directed to securing the necessary foreign exchange for the service of external debt. Such measures further depressed the commodity markets. As prices fell, production was increased in a desperate effort to attain the same income. Heavier export surpluses were thrown on world markets. At the same time, very strong measures were taken to restrict imports, and particularly to protect the peasant production of European countries.

Most of the debtor countries did, in fact, by drastic reduction of imports and some export expansion, achieve a considerable increase in their export balances or a reduction in their import balances in 1929, 1930 and 1931, despite the lower levels of export prices under which they were labouring. Some of the details of this process are dealt with in the *Review of World Trade, 1930*. The most striking development was that of Germany, whose value of imports was reduced by 25.8 per cent between 1928 and 1930, while the value of exports rose by 9.8 per cent in 1929 and in 1930 remained only 2 per cent below the 1928 level. In consequence, a large import balance in 1928 was turned into a considerable export balance in 1930. Other debtor countries — the Argentine, Austria, Australia, Brazil, Bulgaria, Colombia, Finland, Greece, Hungary, Lithuania, Poland, Venezuela, are some examples — were forced to the same effort to improve their commodity trade balances.

¹ Sir Arthur Salter, *Recovery*, London, Bell, 1932, pages 51-54.

² *Ibid.*, Part II, Chapter II.

It is noticeable that this change began in many cases as early as 1928 and was most successful in 1929, when good harvests were a help in many countries. The collapse of prices in 1930 in most agricultural countries neutralised the increased exports (and the import restrictions), dragging down the balances of trade in that year to less favourable positions. The improvement of trade balances up to the third quarter of 1931 was caused mainly by the application of economic pressure exercised through the restriction of domestic credit. But even in 1929 and 1930 there were cumulative tariff increases, and after the abandonment of the gold standard by many countries in the latter months of 1931, extraordinary measures were taken to regulate foreign balances.

In the great creditor countries the reverse movement took place. In the United States of America the active export balance over imports was considerably reduced; Great Britain, France and other creditor countries increased their import balances.

It is obvious that such large shifts in the balances of trade entailed dislocation of existing organisation. The capacity of the borrowing countries to purchase manufactured articles, no longer sustained by heavy capital imports, fell off very considerably. For a time the sustained prices of manufactures, as compared with raw materials, enabled European countries to maintain their trade much more satisfactorily than was possible for the raw-material-producing countries outside Europe. The share of Europe in world trade was substantially increased.

But even in Europe, and in other areas also, the deepening of the agricultural crisis and the increased export surpluses of debtor States created a dangerous tariff situation. It will be shown later¹ that, as early as 1929, many of the raw-material-producing countries had increased their tariff duties in a double effort to gain revenue and restrict imports. The great tariff event of 1930, however, was the passing of the Hawley-Smoot tariff in the United States, by which additional duties were imposed on more than 900 items. The greater number of the heavier duties were imposed upon manufactured articles, so that the exports of European countries, and particularly of Germany, to the United States were most affected. Europe is on balance a large debtor to the United States and, in default of new loans being available or of direct payment by exports of manufactured articles, the European countries must seek to mobilise dollar resources by exporting to other markets, which in turn receive

¹ See Chapter X.

payment from the United States for their exports. The transaction, at its simplest, must be three-cornered, the European debtor country exporting manufactures to a raw-material-producing country which in turn can export to the United States. But in 1929 and 1930 these raw-material countries were in serious difficulties, the supply of new capital fell off during 1929 and, when the United States tariff further restricted the possibilities of direct payment of debt obligations, it was not feasible to increase exports of manufactured goods to neutral markets. The result was a further very heavy pressure upon prices in the debtor States, or, more precisely, upon their export prices. Moreover, the United States tariff was the precursor of many others, and by the end of 1930 there was a serious constriction of international trade, still further outlining the difficulty of discharging debt obligations.

The deepening of the economic crisis throughout the latter months of 1930, therefore, was due largely to the accumulating difficulties of the debtor countries, and particularly of those among them which relied primarily upon exports of raw materials and foodstuffs. There were many complications, perhaps the most important being the continued attraction of the French short-term balances back to France and the imposition of the Hawley-Smoot tariff. The former was accompanied by a continued drain of gold to France, and not only weakened the financial position of other gold-standard currencies, but hindered any large possibilities of renewed long-term capital exports from the United States and Great Britain. The latter still further hampered the free exchange of commodities by which alone the heavy payments on account of debt service might have been achieved. These and many other complications, some political, others economic, making for credit stringency and insecurity, steadily aggravated the already difficult problems of international finance. Efforts at recovery, made, particularly in the United States, in the spring of 1930 and again in the spring of 1931, were dragged down by the continuous fall of raw-material prices and the plight of the debtor countries.

The strain and insecurity of the year are well illustrated both by gold movements and by the violent fluctuations of short-term capital, together with the great shrinkage of long-term international investment.

Some of the more significant statistics are summarised in the following table :

Capital Movements and the Movement of Gold, 1928-1930.
\$ (000,000's).

Country	Year	Capital movement : direct estimates		Total balance	Indirect estimates (balance on account of goods, services and gold)	Gold movement	
		Long-term balance	Short-term balance			Balance of imports	Balance of exports
(+ = inward, - = outward balance)							
United Kingdom ¹	1928	..	..	..	— 569	24	..
	1929	..	..	..	— 574	..	73
	1930	..	..	..	— 112	24	..
United States . .	1928	—727	—386	—1,113	—1,099	..	392
	1929	—272	+ 24	—248	—206	175	..
	1930	—236	—334	—570	—196	280	..
France ²	1928	..	..	..	— 236	254	..
	1929	..	..	..	+ 20	337	..
	1930	..	..	..	+ 252	460	..
Germany ³	1928	+426	..	..	+1,007	218 ³	..
	1929	+157	..	..	+ 553	..	105
	1930	+367	..	..	+ 148	..	14

Unfortunately, the data available are still far from complete for most countries. In particular, it is not possible to get adequate information concerning the movements of short-term capital in these years. That they were violent may be inferred from the fluctuations in the estimates shown above for the United States and Germany. There were withdrawals of short-term balances on a considerable scale from Germany in 1930, at the same time as large temporary advances were extended. A transcript of this section of Germany's international balance-sheet gives an illuminating picture of the complications involved in the necessity of raising a considerable volume of fresh short-term loans to protect the currency, while there was at the same time a steady withdrawal of private deposits.

¹ The figures for the capital balance exclude Government capital transactions.

² The figures for the capital balance exclude amortisation of inter-Allied debts.

³ The figures for long-term capital are incomplete.

Capital Items in Germany's Balance of International Payments, 1928-1930.

Reichsmarks (000,000's).

Items	Inward or credit capital movements			Outward or debit capital movements		
	1928	1929	1930	1928	1929	1930
I. Long-term Operations.						
1. Amortisation payments, including repurchases of domestic bonds	—	—	—	100	111	130
2. Other purchases and sales of existing bonds	2,276	1,546	1,013	1	1	1
3. Purchases and sales :						
(a) Of domestic shares				—	1,361	1,175
(b) Of foreign shares				1,846		
(c) Of real estate in the country	14	7	—	57	17	—
4. New capital issues (net proceeds)	1,341	321	1,058	14	19	63 ^a
5. Release of German property in United States of America	147	275	800	—	—	—
6. Other long-term investments	27	19	39	—	—	—
II. Short-term Operations.						
7. Change in the gold deposits of the Reichsbank abroad	—	—	—	5	64	72

8. Increase or decrease :						
(a) In foreign deposits in German banks	1,914	987	—	—	—	428
(b) In the foreign exchange holdings of the banks of issue	—	—	52	65	281	—
(c) In foreign assets of other German banks	—	—	56	693	438	—
9. Short-term loans and credits raised and repaid	173	389	1,135	111	45	572
10. Increase in cash balances of the Reparation Agent	62	199	—	—	—	167 ³
11. Other known movements of short-term capital	21	—	—	31	—	—
III. <i>Undefinable Capital Movement.</i>						
12. Undefinable net import or export of capital ⁴	1,175	915	—	—	—	923
Total	7,150	4,658	4,153	2,922	2,336	3,530
Net inward (+) movement of capital	+ 4,228	+ 2,322	+ 623			

¹ Included with item 3.

² Participation in the Bank for International Settlements.

³ Decrease in balance.

⁴ The figures entered against this item are not based on direct evidence (cf. *Balance of Payments, 1930*).

It is, unfortunately, not possible to illustrate the position of other debtor countries in this way ; but the remarkable movements shown above for Germany are perhaps sufficiently indicative of the violent fluctuations in capital movements in 1930.

(iii) THE FINANCIAL CRISIS, 1931-32.

In the spring of 1931, as in the spring of 1930, there seemed to be a definite easing of economic and financial conditions. The early months of the year were calm, there was some return flow of capital to Germany and of gold to Great Britain, security prices rose somewhat in most countries in the spring, and money-market rates were extremely easy in the chief financial centres. The Bank of England rate stood at 3 per cent in January, the rates in Paris and Zurich were lowered to 2 per cent in that month, and on May 7th, the New York rate, which also had stood at 2 per cent, was further lowered to $1\frac{1}{2}$ per cent, enabling the Bank of England to reduce its rate again to $2\frac{1}{2}$ per cent, the lowest point since the war. During the first five months of the year, with the one significant exception of India, where the rate was raised by 1 per cent in January,¹ all the changes in official bank rates were downward. There was ample evidence, therefore, of monetary ease in the chief creditor countries, and of the accumulation of liquid capital funds.

In past crises, such conditions in the principal money markets have always been the precursor of recovery from depression ; but in 1931 the financial weakness of the borrowing countries, and of borrowers within the industrial countries, was such that improvement did not follow. It is significant that none of the debtor countries, with the exception of Roumania on April 1st, was able to reduce its discount rate. Meantime, prices, particularly of raw materials and foodstuffs, continued to fall steadily. The financial crisis which followed made it abundantly clear that it was the plight of the debtor countries, at once a main cause and the consequence of falling commodity prices, that was the darkest spot in the almost universal depression. Only Soviet Russia and China, which were insulated to some extent — the former by its planned and closed economy, the latter by being on a silver currency — escaped the worst effects of falling prices.² In both these cases, however, the fall of prices on world markets caused difficulty through the lowered receipts from their export trade. Elsewhere the heavy financial burdens, high rates of interest, increasing risk premia³ and the continuous

¹ The Indian rate was lowered again on May 28th.

² See *The Course and Phases of the World Economic Depression*, pages 239-246.

³ *Ibid.*, page 303.

narrowing of international markets, together with the rapid and severe decline of prices, brought increasing financial stringency.

The plight of the borrowing countries, reinforced by their failure to secure new capital imports,¹ was inevitably reflected in considerable shrinkages of their national incomes and purchasing power. This caused a further decline in their imports and neutralised the possibility of industrial revival in the creditor countries, whose conditions were further affected by the steadily growing volume of unemployment. The discrepancy between raw-material and industrial prices described in Chapter IV was a material factor in preventing improvement in this situation. The volume of agricultural production did not fall appreciably, and there was heavy pressure particularly on the prices of the export surpluses seeking world markets. On the other hand, the prices of manufactured products were relatively well sustained and production fell to very low levels. Savings piled up but investment fell off, and very large amounts of credit were held at low rates of interest on short term. On the other hand, long-term rates of interest remained relatively high.

Failure to correct these maladjustments negated the hopes that had been placed upon the progressive cheapening of short-term credit. The New York discount rate remained at 1½ per cent, the lowest rate ever quoted, from May 8th to October 9th, 1931, gold reserves were ample and the expansive possibilities of the Federal Reserve system undiminished, but it did not prove possible to "pump credit into the markets". Several factors blocked the way, of which probably the most important were political insecurity, leading to fear for the safety of international investments; the weak position of the London money market, which before the war was the main distributor of such investments; the failure of either the New York or Paris markets, which were stronger, to take London's place in this respect; the resistance to curtailing production of agricultural products and to reducing costs and prices of manufactures; long-term rates of interest maintained at levels too high for investment to be profitable; and, most immediately important of all, the over-borrowed state of many debtor countries. There was a block in the circulation of capital which could not be removed merely by lowering the short-term rates of interest.

The various difficulties enumerated were rendered more troublesome because they were interlocked. The block in circulation, first of capital and then of goods, was comparable to

¹ There had been an actual export balance on capital account in the second half of 1930 in some of these countries and a considerable reduction of imports in most, together with higher rates of interest.

a jam in logging operations on a river. Circulation could have been restored only by finding the key logs and liberating them almost simultaneously before another jam could form. The high rate of long-term interest, for example, originally established by the scarcity of capital and strong demands for reconstruction after the war, was maintained by the boom in investment and the security speculation which was described earlier in this chapter. After these demands failed in 1929, the rate was still kept up by borrowers who were prepared to pay interest higher than that which could have been paid if the capital had been used profitably in industrial production. This "distress" borrowing, based upon the effort to maintain the solvency of already excessively burdened debtor countries, was the actual point upon which the financial crisis broke.

The interlocking of economic, monetary and political factors is particularly well illustrated by the heavy borrowings on long term at high rates of interest, by Governments and banks, "not for investment in productive enterprise, but to build up liquid reserves, partly gold and partly foreign balances, with which to protect their newly restored currencies"¹ This process, by which it has been estimated £500 million was borrowed in the New York market in 1927-28 on long term and re-deposited on short term mainly by European countries, gave that market a plethora of short-term funds (which was part of the basis for the security boom) while helping to keep the long-term interest rates at levels which checked productive investment.

In May 1931, while money rates were still easy and there was still some measure of faith in a speedy recovery from the depression, a large Austrian bank, the Creditanstalt, disclosed heavy losses. The importance of this news from Vienna, which travelled round the world's financial centres like a seismic shock, lay less in the event than in its general significance.² It was instantly realised that, not only other banks in Austria and foreign countries, but virtually the whole industrial structure of Austria, and other Eastern European countries, would be involved. It was equally evident that neighbouring debtor States, and particularly Germany, would be at once exposed to the danger of panic withdrawals of capital. A crack had developed in the carefully constructed and patched façade of international finance and, through that crack, already timid investors and depositors caught glimpses of a weak and over-burdened structure. It was not only a bank which threatened to collapse, but the whole system of over-extended financial

¹ Cf. J. M. Keynes, *The Future of the Rate of Interest*, Index, Vol. V. No. 57, September 1930.

² Cf. the graphic account given by Sir Arthur Salter, *Recovery*, Chapter IV.

commitments which was the worst legacy of the war and of subsequent credit expansion.

Austria had been the first European State, except Sweden, to stabilise its currency and undertake a comprehensive policy of reconstruction. The success of that policy was the earliest, and in many respects the most convincing, proof of the efficacy of international co-operative action in the financial and economic sphere. It was, moreover, both a model upon the experience of which subsequent reconstruction schemes drew heavily, and a material factor in promoting the recovery of industrial production and trade which was worldwide after 1925.¹ When, in June 1926, the League Commissioner laid down his office, financial stability had been restored and competent economic investigation had given reassuring evidence of sound economic recovery.² The economists' report, however, drew attention to the dependence of Austria upon external commercial conditions and her vulnerability to tariffs, to the necessity of maintaining the foreign credits that had been obtained, and to the danger that might arise from her "swollen banking apparatus, too large for her present needs". The main drift of the economists' report was summarised in the statement that "the factor which will decide whether Austria remains in poverty or is able to recover to a more normal standard of comfort is her ability to sell her goods abroad".³

During the boom period 1926-1929, private capital flowed into Austria, as into the other Central and Eastern European countries, in considerable volume. Industrial, commercial, banking and State enterprises were extended and heavy debt liabilities were built up. The first indication of the extent to which the banking and industrial structure of Austria had become dependent upon the continued flow of new capital came in October 1929, after the curtailment of capital exports from the United States. The Boden Creditanstalt, a large industrial and agricultural bank, became embarrassed and was absorbed by the Creditanstalt on terms which represented a severe loss to the shareholders. The Creditanstalt, itself deeply committed with industrial investments, by absorbing those of the Boden Creditanstalt and two other banks, was in a weak position when the full force of the world depression burst upon it in 1930. In that year it suffered a loss of 140 million schillings (\$20 million), so that in May 1931 the Austrian Government, in order to avert

¹ *The Financial Reconstruction of Austria*, (document C.568.M.232.1926.II).

² *Report by Mr. W. T. Layton and Professor Charles Rist on the Economic Situation of Austria* (document C.440.M.162.1925.II).

³ *The Financial Reconstruction of Austria* (document C.568.M.232.1926.II), page 244.

a breakdown of the banking system, was forced to guarantee all deposits, foreign and domestic, of the bank. In this operation it was assisted by an advance of 150 million schillings from the Bank of England, while at the same time the Bank for International Settlements advanced 100 million schillings to the National Bank of Austria.¹ The foreign creditors of the Creditanstalt, for their part, undertook not to withdraw their advances, amounting to 500 million schillings, for a period of two years.²

For the time being, the situation in Austria was saved. The subsequent history of the Creditanstalt became merged with that of the National Bank of Austria and the Austrian Government. On August 7th, the latter addressed a letter to the League of Nations requesting the Council "to proceed to an examination of Austria's economic and financial difficulties and to seek the means of remedying them". When the Financial Committee of the League met in September, Hungary also had requested assistance. Greece and Bulgaria followed in January 1932, and in March of that year the League was faced not only with the specific situations in those countries, but with the general problem of the financial and economic structure of Eastern and Central Europe in relation to the world depression.

Before these developments took place, however, the storm-centre had shifted, first to Germany, then to England, and later to the United States. The revelation of financial weakness in Central Europe created a panic among investors and holders of short-term balances. As early as September 1930, the Reichsbank had suffered a run. Political conditions were disturbed and there was fear of a revolution. The reserves of the Reichsbank fell alarmingly as securities were sold and short-term credits were withdrawn to the extent of almost RM. 1,000 million (\$250 million) in the last quarter of the year, 10 per cent of the foreign exchange holdings being lost in a single day. The run was temporarily stopped by an international banking group advancing \$125 million for six months, with the possibility of three renewals.

The Austro-German protocol announcing the plan of a Customs Union appeared on March 21st, 1931. The European political situation was strained and international economic co-operation became more difficult. Soon after the Creditanstalt difficulties were announced, a renewed run began on the Reichsbank, which lost \$250 million of its gold and foreign exchange in four weeks. The Bank for International Settlements,

¹ The Austrian Government had successfully floated a loan of \$102 million in July 1930.

² League of Nations Financial Committee : Report to the Council, September 19th, 1931 (document A.55(b).1931.II.A).

on June 25th, arranged a rediscount credit of \$100 million to help the Reichsbank ; but three-fourths of this credit was used in a month.

Meantime, the President of the United States launched, on June 23rd, the proposal for a year's moratorium of reparation and war-debt payments. On July 6th, the proposal went into force amended by an arrangement under which Germany agreed to pay the unconditional annuities to the B.I.S. and France agreed to reinvest them in guaranteed bonds of the German State Railways. The relief thus given to Germany did not, however, stay the course of the panic. On July 8th, an emergency decree was issued in Berlin under which effect was given to a joint guarantee by banking, industrial and trading establishments of RM. 500 million to be placed at the disposal of the Gold Discount Bank in order to sustain foreign credits. Withdrawals of foreign exchange continued, however, and the disclosure of enormous losses by the North-German Wool Company involved the closure of the Danat (Darmstädter und Nationalbank) on July 13th, despite a Government guarantee of its liabilities on the previous day. Other German banks were subjected to runs and were compelled to limit withdrawals to from 5 to 20 per cent of deposits. The Bourse was thereupon closed, the discount rate rose from 7 to 10 per cent and the statutory reserve ratio of the Reichsbank was lowered from 40 to 30 per cent. At the same time, provision was made for control of foreign exchange payments to be centralised in the Reichsbank and for restriction of bank payments.

International effort was continued. The British Government announced that it would not require payment of its share of the reparations due on July 15th, and the B.I.S. next day renewed its rediscount credit to the Reichsbank. An international conference was held in London from July 20th to 23rd,¹ which invited the Bank for International Settlements to "set up without delay a committee of representatives nominated by the Governors of the Central Banks interested, to enquire into the immediate further credit needs of Germany and to study the possibilities of converting a portion of the short-term credits into long-term credits".

This Committee met at Basle on August 8th, and proceeded to a careful detailed study of the German situation.² The report stated emphatically its agreement with the opinion of the London Conference that the withdrawals of short-term balances were

¹ Attended by representatives of the United States, Belgium, France, Germany, Italy, Japan and the United Kingdom.

² Report of the Committee appointed on the Recommendation of the London Conference, 1931.

“not justified by the economic situation of the country”. Withdrawals had, however, taken place, and the large volume of short-term liabilities still remaining rendered Germany extremely vulnerable. Germany, at the end of 1930, had short-term investments abroad amounting to about RM. 5,300 million but her foreign short-term indebtedness was estimated at RM. 10,300 million. As in Austria and the other borrowing countries, the bulk of this indebtedness on short-term was on private, mainly banking account. “RM. 1,100 million consisted of the short-term debts of the Reich, Federal States and Municipalities, RM. 9,200 million of the obligations of the banks and the balance of other short-term liabilities.”¹ The seriousness of the drain is illustrated by the fact that, in the first seven months of 1931, no less than RM. 2,900 million were withdrawn, of which RM. 2,100 million came from the short-term liabilities of the banks.

It was for this reason that arrangements were made for a meeting of the foreign banking groups concerned, from August 14th to 19th, with the result that a “standstill” agreement was arranged “for the continuation of credits to the German debtors up to the total then outstanding for a period of six months, subject to an arrangement being made with regard to the existing central bank credits”. Similar standstill agreements were made by the creditors of other debtor countries such as Austria and Hungary. When the German agreement expired in February 1932, it was possible, after prolonged negotiations, to arrange a further renewal, subject to the repayment of 10 per cent of the outstanding total.

The second half of the Committee’s task required it “to consider the possibility of Germany raising a long-term loan”; but the Committee pointed out the dependence of any such proposal upon “the assurance that international political relations are established on a basis of mutual confidence, which is the *sine qua non* of economic recovery, and that the international payments to be made by Germany will not be such as to imperil the maintenance of her financial stability”. Their report concluded on a note of urgency, printed in heavier type “urging most earnestly upon all Governments concerned that they lose no time in taking the necessary measures for bringing about such conditions as will allow financial operations to bring to Germany — and thereby to the world — sorely needed assistance”.

As a result of these emergency measures, the danger of imminent collapse in Germany seemed to have been tided over. Immediately after the London Conference, it was announced

¹ Report *op. cit.*, page 3.

(on July 25th) that the Danat Bank would be reopened. On August 1st, the bank rate was raised from 10 to 15 per cent; but after the renewal, on August 3rd, of the B.I.S. credit of \$100 million, the Reichsbank gained gold and foreign exchange cover. The rate was reduced again to 10 per cent on August 12th, and 8 per cent on August 19th. On the latter date also the "standstill" agreement was signed with the Bankers' Committee; the stock exchanges reopened on September 3rd, on the same day as it was announced that the proposal for an Austro-German Customs Union would be dropped. The strain was not renewed until after the fresh disturbances caused by Great Britain's abandonment of the gold standard on September 21st.

(iv) THE ABANDONMENT OF THE GOLD STANDARD.

Great Britain's difficulties were connected both with Germany's and with those of Central Europe, which were very much aggravated by the run on German banks. The movements of bank rates in June, July and early August were all upward. The Bank of England raised its rate from $2\frac{1}{2}$ to $3\frac{1}{2}$ per cent on July 23rd and to $4\frac{1}{2}$ per cent a week later. Despite this action, it lost over £30 million in gold in the last fortnight of July. It was known that British bankers had lent, not only Germany, but other Central European countries, a large amount of short-term credit which was rapidly becoming "frozen" by the inability of these countries to meet their foreign obligations. The Macmillan Committee, in its report published on July 13th, had drawn attention to the volume of short-term claims on London and, even though it was pointed out that the amount had fallen, some uneasiness was created by the magnitude of the total. On July 31st, the May Committee published its report upon the condition of the public finances, and for the first time there was general realisation of the probability of a large deficit, estimated at £120 million. The Cabinet disagreed on proposals to balance the budget, and on August 24th the National Government was formed.

At the beginning of August, the Bank of England had secured a credit of £50 million from French and American banks, with which to withstand the drain on the gold reserves caused by the withdrawal of short-term balances and the sale of British securities. On August 29th, a further credit of £80 million was arranged by the Treasury; but the drain continued. Over £200 million was withdrawn from the London money market in the two months preceding September 20th. A supplementary budget imposing heavier taxation was introduced on September

10th as a measure of financial reform ; but on the 15th, a protest by naval ratings in the Atlantic Fleet against pay reductions was given wide publicity. The run on London rose to extraordinary proportions. Between Wednesday morning, September 16th, and Saturday midday, the 19th, over £43 million of short-term funds were withdrawn. On the other hand, British short-term holdings amounting to £70 million in Germany alone had been locked up by the London Conference Agreement. On September 21st, therefore, legislation was passed suspending the Bank of England's obligation to sell gold. The bank rate was raised to 6 per cent and the Stock Exchange closed for two days, while restrictions were imposed temporarily upon dealings in foreign exchange.

The immediate effect of this momentous decision in Great Britain itself was not alarming. As soon as the Stock Exchange opened, there was a small boom in the sterling prices of industrial securities. Exchange rates on gold currencies dropped 25 per cent almost immediately ; but prices in Great Britain remained steady and the people were calm. The National Government appealed to the country, and was given an overwhelming majority on October 27th. There was no longer any doubt about the necessary financial measures being taken to balance the budget, and, in fact, these measures proved more fruitful than had been expected. As domestic prices remained steady, tension gradually relaxed. On October 30th, the Bank of England repaid £20 million of its first loan from the French and American banks, the remainder being renewed for three months. At the expiration of this period, the balance was met. The greater part of the Treasury Loan (\$150 million and Fr. 1,600 million) was repaid at the end of February, the remainder of the American portion (\$50 million) being repaid at the end of March, thus wiping out the advance, with the exception of a part of the French loan, which was in a form that could not be redeemed in advance.

The inherent financial strength of Great Britain was also displayed in the fact that the mere cessation of overseas lending once again enabled her to draw resources from her debtors all over the world. Imports increased heavily and a series of measures, beginning with the Abnormal Importation (Customs Duties) Act of November 19th, was taken to restrict them. Exports of gold from India, tempted out of hoards by the premium in terms of rupees, flowed in increasing quantities to Great Britain and were a material help in enabling the Bank to pay off its foreign credits.¹ Essentially the process was a

¹ For an estimate of this movement, see Report of the Gold Delegation of the Financial Committee, Geneva, 1932, League of Nations (document C.502.M.243. 1932.II.A), Section IX, "The Supply of Monetary Gold".

mobilisation of overseas investments, since the Indian Government used the gold offered to it to pay off maturing loans. Finally, the strong creditor position of Great Britain began to exert its influence upon the exchange rates, despite the large repayments to France and the United States. The pound was undervalued, and, when it began to rise, speculation assisted the process. From the 30 per cent discount to which it had dropped in February, sterling recovered quickly to less than 20 per cent discount in April. Bank rate was lowered to 5 per cent on February 18th, to 4 per cent on March 9th and to 3½ per cent on March 16th, the upward swing of the exchanges was checked but sterling remained strong.¹

Elsewhere, on the other hand, the repercussions of the fall of the pound were more serious immediately. The first effect was to cause the abandonment of the gold standard by a number of other countries which were in close relationship with Great Britain. The Argentine and Uruguay had suspended gold payment in December 1929, Canada had introduced restrictions on the gold standard at the end of 1929 also, and in 1930 the exchanges of Brazil, Chile, Venezuela, Paraguay, Peru, Australia and New Zealand fell and remained below export gold point. After Great Britain's action, the number of countries off gold was greatly increased. Before the end of October 1931, all the British Dominions except South Africa, the rest of the British Empire, and the three Scandinavian countries, as well as Portugal, Egypt, Bolivia, Latvia and Finland, had departed from gold. Japan followed in December 1931, Greece in April and Siam and Peru in May 1932.

This very considerable breakdown of the world's monetary mechanism was important in itself. Even more important in the immediate situation, however, was the reaction upon the remaining gold standard countries and upon the financial structure of the world as a whole. When Britain went off gold, all the European stock exchanges, except those of Paris, Milan and Prague, closed for various periods; bank rates rose, foreign exchange restrictions (ranging from limitation of imports to moratoria)² were imposed in thirty different countries, tariffs were increased, contingent, priority and quota systems introduced.²

Partly as a result of these trade restrictions, the financial storm burst with redoubled force on Germany, which on November 19th applied to the Bank for International Settlements for the convocation of the consultative Committee provided for by the Young Plan. The Committee met at Basle on December 7th, and

¹ The rate was further reduced to 3 per cent on April 21st, and 2½ per cent on May 12th.

² See Chapter X.

next day the German Government published an Emergency Decree, the fourth of a series, effecting sweeping economies in the public service, heavier taxation, salary, wages, rent and price cuts and economies in unemployment insurance. There was no precedent, outside of Russia, for such drastic measures both of control of economic life and of sacrifices imposed on a whole people. The Committee, in support of its conclusion that Germany, after the expiry of the Hoover Moratorium in July 1932, would not be able to provide the "conditional" reparation payments under the Young Plan, made a thorough investigation of the developments since the Advisory Committee of the London Conference had reported in August. It found that "the total commercial debt, and in particular the amount lent on short-term", was larger than the earlier estimate, amounting to nearly RM. 12,000 million at the end of July 1931. Of this total, however, RM. 4,000 million were non-banking credits and therefore less liable to be withdrawn, while RM. 6,000 million were under the standstill agreement. It was significant that, of the amount not covered by the standstill agreement, RM. 1,200 million had been withdrawn by November 20th. The renewal of the standstill agreement in February 1932, and the extremely vigorous measures of deflation within Germany itself, kept the currency stable and the acute stage of the panic passed once more. In the spring of 1932 there was relative economic calm, but on a basis of lower prices, higher unemployment, and greatly shrunken trade.

Before the acute stage of the panic passed, however, New York was for a few weeks subject to much the same kind of run as London and Berlin had experienced. In October, a "gold rush" set in which had the net effect of reducing the United States stocks by \$715 million. For a time there was some discussion of currency stability; but, beyond its effect on timid investors and depositors and through them upon bank failures, this discussion had little reality.

France also did not go unscathed in the panic. After the depreciation of the pound sterling, a number of banks were forced to close down. The Government came to the rescue of the Banque Nationale de Crédit and also made special arrangements with the Banque de France covering its losses on sterling holdings.

The most important results of the British action, however, were slower. The panic passed, and in the spring of 1932 there was lethargy — a state of suspended animation — rather than feverish action. But in the meantime the fundamental difficulties of the crisis were sensibly aggravated. The apparent stability of prices in the countries that had abandoned gold contrasted

strongly with the precipitate further decline of gold prices. Foreign investment, which had been reduced before, in the latter part of 1931 became negative as the great creditor countries ceased lending and drew upon their vast resources. Trade circulated more feebly than ever in the face of continually increasing restrictions. Standstill agreements imposed a virtual paralysis upon a growing part of international finance.

Statistics are given in Chapter VI of the extent to which the flow of capital from creditor to debtor countries has been reversed in the depression years.

Such violent reversals of the normal flow of capital movement, involving altogether unprecedented gold shipments and accumulations, have completely disorganised world trade. The world's creditors have not only stopped lending, but have been drawing in both interest and capital as far as that has been possible. The international economic situation thus created is comparable only with that which would result if all the banks in a developing mercantile community were to refuse new accommodation, and press for both interest payments and reduction of overdrafts.

Throughout 1931 and the first half of 1932, Europe held the centre of the stage, with only occasional attention diverted to the United States. But the financial situation of the rest of the world for the most part grew steadily worse also. Japan affords a good example of the strain. Prices fell in that country from 228 in January 1929 and 201 in January 1930 to 159 in January 1931 and 147 in November 1931, after which Japan left the gold standard. Exports fell off from Yen 2,218 million in 1929 to Yen 1,179 million in 1931, while imports were virtually halved also. In the invisible trade a surplus of Yen 220 million in 1928 had become a deficit of Yen 15 million by 1931. Earnings fell practically 10 per cent in 1931 and employment declined in approximately the same degree. In the first eleven months of 1931, Japan lost almost 40 per cent of her gold reserves, and this after she had lost 25 per cent in 1930. Her reserve, which had been Yen 1,087 million on January 18th, 1930, fell to Yen 521 million on December 5th, 1931.

Other examples might be quoted; but, with the possible exception of Australia after the abandonment of the gold standard by Great Britain, there is a consistent story of unrelieved deepening of the depression. In Australia, a currency already 30 per cent below sterling shared in the sterling fall also. Tariffs had been raised, wages, salaries and domestic interest had been reduced, and even the slight rise in sterling prices brought some relief. There was, indeed, some softening of the shock in all the countries which had followed Great Britain off gold; but, since this action

was not universal and its immediate effect was to precipitate a still further decline in gold prices and to concentrate the deflation still more heavily on the gold-standard countries, the restrictive measures introduced to cope with this situation engendered so much deeper depression that not even the countries which had abandoned gold could wholly escape further contraction. In the spring of 1932, Europe and the world as a whole lay prostrate and exhausted by a succession of disasters; but there was little indication that any of the restorative measures proposed were capable of restoring its vigour.

Chapter III.

THE DISORGANISATION OF PRODUCTION.

(i) THE CHANGING STRUCTURE OF WORLD PRODUCTION.

The basis of the world's work is individual effort. Despite scientific discoveries and mechanical contrivances, the bulk of the world's production is still carried on from year to year by comparatively simple processes and on a small scale. A superstructure of manufacturing production has been erected upon the foundation of the extractive industries, and an elaborate organisation of commerce and credit has become necessary for the whole system. In the last analysis, however, the production of foodstuffs and raw materials is not only the primary process, but may if necessary become the basis of a simpler, less extended and less intricate economic organisation supporting a lower standard of living.

In modern times, not only the superstructure of manufacturing, but the commercial and credit organisation — all the secondary and tertiary processes of economic production — have come in most countries to play an increasingly important rôle. Moreover, the widespread and complex organisation has called for increasing attention to the co-ordination of individual and group activities. The organisation of co-operation demands a larger proportion of thought and effort, and many specialised parts of the organisation become somewhat remote from the actual productive processes. The fundamental reason for the existence of commercial and banking institutions lies in their utility in facilitating co-operation among producers and consumers; but such institutions tend to take on a life of their own, to exercise a directive control over production, and, by their own difficulties, to exert at times a disturbing influence on productive activities. It needs, therefore, to be remembered, especially in times of crisis, that economic activity is designed primarily for efficient production, and that the production of

foodstuffs and raw materials is the first and most essential stage in the process.

It is, moreover, the most stable and reliable part of the economic organisation. As was recorded after a previous depression, seed-time and harvest, cold and heat, summer and winter, do not cease, even in times of acute economic crisis. It is the superstructure rather than the foundations of economic life which is shaken by most crises. Indeed, the crises have often arisen from the unsatisfactory operation of the commercial and credit mechanism ; though at times a disequilibrium between the demand and supply of agricultural products plays an important part.

The records of most previous crises are remarkable for the comparatively slight variation they disclose in the quantity of production. Statistics do not extend very far back and are not very complete for most countries. Perhaps the most elaborate are those for the United States of America, a country which has experienced an unusually rapid and sustained economic expansion.¹ Even when the upward trend of the statistics is eliminated, however, the degree of fluctuation of productive activity in economic booms and depressions is comparatively small. Some evidence of this was collected in a previous League publication.²

Most recent depressions, those for which fairly adequate records are available, were quite clearly concentrated in, though not confined to, the credit and commercial structure. The liquidation and reorganisation which they caused necessarily extended into the productive organisation, but mainly into the secondary manufacturing processes. Aberrations in the mechanism shook the superstructure and perhaps caused some strains and breakages before it settled to a new equilibrium, but the foundations of economic life were less affected. The basic curves of the production of raw materials and foodstuffs, indeed, show remarkably constant movement. There are, from time to time, important changes in the production of individual commodities or groups of commodities ; but the general trend of production appears to have been affected only to a minor degree by fluctuations in business activity.

This is even truer of foodstuffs and agricultural than of mineral raw materials, because of the primary and stable demand for food and clothing which they meet and also of the nature of their production. The rapid progress of mechanical methods of manufacturing production tends to obscure the fact that an

¹ Cf. the diagrams shown in Chapter II of Carl Snyder, *Business Cycles and Business Measurements*; New York, Macmillan, 1927.

² *The Course and Phases of the World Economic Depression*, Chapter VII.

overwhelming proportion of the world's population, even in the twentieth century, still lives very close to the land. Not only the vast agricultural populations of Asia, but the peasantry of Europe depend primarily upon the tillage of the soil. Manufacturing production in its highly mechanised forms has until recently been largely confined to a small area of western Europe and North America. It is this urbanised and mechanised part of the world which has suffered most severely in the past from periodic depressions. In proportion as the population has become divorced from the elementary processes of agricultural production has it become more vulnerable to fluctuations in economic activity.

In the present depression, however, there has not only been a greater decrease in production as a whole, but the effects of that decrease have shown themselves more than in any previous depression in almost every branch of economic activity and in every country. Even in previous depressions when the derangement was primarily a credit phenomenon or an interruption of unduly rapid or unbalanced growth in manufacturing production, the disturbance of prices which resulted necessarily affected in some degree the livelihood of the producers of foodstuffs and raw materials.

Moreover, there have been times when substantial shifts in basic production have themselves played a large part in unsettling economic organisation. The opening up of vast new areas of production by improved means of transport in the third quarter of the nineteenth century was equivalent to a shift in the foundations of economic life and played a large part in the especially severe crises of the last period of falling prices from 1873 to 1895.

The very much more violent fluctuations of productive activity in the crises of 1920-21 and 1929 to 1932 are probably to be attributed in part to a similar fundamental disturbance of the world's economic organisation. Some of the evidence for this assumption has already been presented in Chapter I, and further evidence, relating more particularly to agricultural production, will be considered in the next section of this chapter. It has been emphasised that the forces which have tended to modify the basic organisation of the world's economic activity were in operation even before they were accentuated and accelerated by the war. Manufacturing production was growing fast in areas outside western Europe and the application of machine methods and scientific research to farming was well under way before the preoccupation of Europe with other concerns from 1914 to 1918 stimulated their rapid development. The post-war credit expansion which made

possible the reconstruction of European production also contributed further to the rapid expansion of competitive production in other areas. This was particularly true of such a fundamental activity as cereal-growing; the mechanisation of which in North and South America and Australia was greatly facilitated by easy credit conditions.

The present depression, therefore, was caused, not only by an over-expansion of credit and international lending, leading to an unsound extension of the manufacturing superstructure at a time when the world had not recovered from the disorganisation caused by the war, but also by a considerable shift in the foundations of agricultural and mineral production upon which the superstructure was erected.¹ It is this fact which not only goes far to explain the severity of the depression, but accounts also for its intractability. The recuperative forces which have been effective in previous depressions, and particularly the cheapening of credit, have so far proved inadequate to the task of bringing about a readjustment based soundly upon the fundamental alterations that have taken place in the ground-plan of organisation.

The importance of these facts is very clearly illustrated by the position of the cereal and especially the wheat-producing countries. There has, in the last two decades, been an "agricultural revolution". Not only mechanical methods of cultivation and harvesting, but the scientific work of the plant-breeder, the parasitologist, and the soil chemist, and the better organisation of transport and marketing have brought new areas into cultivation, increased the yields, and cheapened the costs of production. The peasant farms of eastern Europe, working under small-scale enterprise, with little machinery, less scientific research, and costly commercial credit and transport organisation, face a greatly increased and more formidable competition. The importance of cereal-growing in the economy of many European States is such that they cannot contemplate with equanimity the irruption of this competition into their markets. Their own production, expanded in the effort to meet their financial obligations and encouraged by the cheap credit which was available to them in the boom period, cannot compete successfully on equal terms with that of the newer mechanised farming-lands. It is difficult for them either to adopt the new methods, or to lower their costs under the old methods. Even with high

¹ Cf. Bertil Ohlin, *Now or Never*, Index Vol. VII, No. 77, May 1932, page 128: "A period of industrial depression set in almost simultaneously with an agricultural crisis due to quite different causes, at a time when the powers of resistance and the stability of the economic situation were, for various reasons, reduced and were much smaller than during the decades immediately preceding the war".

protection it is difficult to absorb their increasing populations in manufacturing production, and their export markets tend to close against them. It is argued later that it was precisely these difficulties of the European agriculturists which led after 1925 to the marked revival of tariffs and other manifestations of economic nationalism.¹

The existence of such problems as these renders it necessary to commence any detailed examination of the course of the depression with an exposition of the changes which it has brought in world production. The previous chapters of this *Survey* have been concerned with a sketch of the background of structural change and instability and its complication by credit inflation and with an outline of the overt manifestations of the depression as it developed from 1930 to the middle of 1932. In this and succeeding chapters an attempt will be made to examine in more detail the underlying realities of economic disorganisation — the confusion into which production, prices, international trade, employment, banking, public finance and commercial policy have fallen. Because of the profound importance in the present crisis of structural maladjustments, a beginning is made with production, but all the phenomena are interrelated and it would be superficial reasoning either to ascribe the depression to any one single cause or to seek a solution of its problems by any simple panacea. The confusion into which the economic organisation has been thrown by an unhappy accumulation of strains in the foundations as well as in the superstructure of industry and the credit and financial mechanism demands a very complex and probably a protracted effort of reconstruction, the basis of which, however, must be a recognition of fundamental structural changes.

(ii) STATISTICS OF WORLD PRODUCTION.

Since so large a part particularly of the agricultural production of the world is carried on by individualistic, small-scale methods, it is possible to gain an understanding of the main trends of development only by using such statistics of world production as are available. The statistical material fortunately tends to become more abundant and to improve in quality; but there still remain very large gaps. There is, for example, no adequate information concerning the production of foodstuffs in China, nor concerning the production of forestry products, dairy and poultry farming, fruit and vegetable growing. It is obvious,

¹ See Chapter X, section (ii).

indeed, that the statistics commonly used refer especially to those parts of the world which form part of the developed trading and financial system which links the modern world into one complex organisation. It is, however, in such trading countries that the fluctuations of the depression are most pronounced.

For some years, the Economic Intelligence Service of the League has prepared indices of world production, and in the discussion which follows reliance is placed primarily upon the statistical material thus made available.¹ The first important series of indices calculated in the *Review of World Production, 1925 to 1931*, combine the information available from various sources concerning the production, for the world as a whole and for its main territorial divisions, of sixty-six commodities, which are mainly foodstuffs and raw materials, though a few semi-manufactured commodities are included. The output of manufacturing industry is more difficult to measure; but the *Review* proceeds to bring together various national indices of production and to supplement them by statistics relating to particular important industries. In this connection, an illuminating analysis is given of the differences that emerged, during the period 1925 to 1931, between the production of consumer's goods and that of producer's goods.

Certain significant general conclusions which emerge from the laborious compilation of the mass of statistical information which is necessary for the calculation of such index-numbers may conveniently be set out before entering upon a more detailed examination of the particular groups of commodities. The first table which follows compares, for the world as a whole, the movement of the main indices.

World Production of Various Classes of Goods. ²
(Average 1925 to 1929 = 100.)

	1925	1929	1930	1931
Foodstuffs	97	103	101	99
Raw materials	92	111	101	91
Raw materials for consumer's goods ³	98	104	100	100
Raw materials for producer's goods ³	91	113	98	82
Weighted average of production indices of 12 industrial countries ³	91	112	97	84
International production index (Insti- tut für Konjunkturforschung) ⁴	93	112	101	85

¹ Cf. successive issues of the *Memorandum on Production and Trade*; since 1932, *Review of World Production*.

² For further details, see *Review of World Production, 1925 to 1931*.

³ Excluding the Union of Soviet Socialist Republics.

⁴ See *Vierteljahrshefte zur Konjunkturforschung*, 6. Jg., Heft IV, Teil B, 1932.

The indices shown above, even when their limitations are fully considered, reveal in broad outline certain important tendencies. The first is the extent to which the fluctuation of production has been concentrated in the manufacturing industries.

There is no possibility at present of obtaining a fully representative index of world production including manufacturing output, so that the measures of production given above are not complete. The position of the Union of Soviet Socialist Republics further complicates the problem of measurement, since there has been a rapid advance in industrial and agricultural production in that country even during the depression. The situation in Soviet Russia is, however, so different from that of the rest of the world that it demands separate treatment.

The nearest approaches to measurements of manufacturing activity are contained in the second and the last three indices cited. As will be shown later,¹ it is probable that manufacturing production fluctuated even more widely than the last two indices suggest.

A second fact of some importance is the very marked rise shown in these indices during the boom period, which, however, has been more than counterbalanced by the sharp curtailment of production in the depression.

The relatively stable production of foodstuffs, which is reflected also in the index of raw materials for consumer's goods, stands out in clear contrast with the more fluctuating industrial production.

In considering the significance of these indices, it should be remembered that the continuous increase in world population and in productivity has for many decades resulted in a substantial and cumulative annual average increase in world production. In the present depression, as in the war period, the falling-off of production should be measured in relation, not to the highest point actually reached, but to the point which might have been reached if the normal rate of increase had been maintained.

The geographical distribution of the decline in production during the depression further supports the inference which may be drawn from the figures cited above, that the decline is greatest in the manufacturing countries. The next table shows how marked the differences have been in different areas.

¹ See section (iv).

*General Indices of Production of Foodstuffs and Raw Materials,
weighted by 1930 Values.*

(Basis: Average for 1925 to 1929 = 100.)

Continental groups	1925	1929	1930	1931 ¹
Europe (excluding U.S.S.R.)	95	112	103	98
Europe (including U.S.S.R.)	94	110	104	100
North America	96	102	93	88
Latin America	96	104	102	97
Africa	95	108	106	104
Asia (excluding Asiatic Russia) ²	97	105	108	102
Oceania	93	102	110	108
World	95	106	101	96

This table refers to the combined indices of the production of foodstuffs and raw materials. If these indices are considered separately, the position is even clearer, since the production of foodstuffs increased from 1929 to 1930 in Africa, Asia and Oceania and fell in the remaining areas less than did the production of raw materials.³ The indices for raw-material production are reproduced in Section IV and show how greatly the decline of production has been concentrated in the industrial countries.

The various national indices of production, which take account also of manufactures, show the decline even more clearly, as the following selection of indices will show :

National Indices of Production.

(Basis: Average for 1925 to 1929 = 100.)

	1925	1929	1930	1931
Canada	79	121	103	87
United States of America	95	108	88	74
Japan	90	118	110	109
Union of Soviet Socialist Republics	62	143	175	195
Germany	87	112	92	76
Belgium	80	111	93	84
France	88	114	115	102
Poland	84	115	95	80
United Kingdom	99	112	100	85
Sweden ⁴	90	110	106	94
Czechoslovakia	88	115	101	90

¹ Provisional indices, partly based on estimates.

² Excluding production of foodstuffs in China.

³ *Review of World Production, 1925 to 1931.*

⁴ Unofficial index, not covering total production. The figures of the annual official index of total production are : 1925, 87 ; 1929, 117 ; 1930, 116 ; 1931, not yet available.

It should be pointed out also that the yearly figures quoted above tend to minimise the extent of the decline, which has been proceeding rapidly in recent months. Thus the Canadian index in March 1932 stood at 77 as against 126 in March 1929; that for the United States fell in the same period from 109 to 61; the German index fell from 110 to 61; the French, which was 113 in March 1929, remained high till 1931 (standing in March at 108) but fell rapidly to 80 in March 1932. The Polish index also fell from 118 in March 1929 to 61 in March 1932.¹

The only exceptions to this story of continuous and accelerated decline, as far as the industrial countries are concerned, are those countries which, like the United Kingdom, abandoned the gold standard in the latter part of 1931. The British index, which stood at 110 in the first quarter of 1929, fell rapidly in 1930 and by the third quarter of 1931 stood at 82; but recovered and, in the first quarter of 1932, had risen to 93. Sweden shows much the same general tendency, though the decline of production in that country up to the third quarter of 1931 and the subsequent recovery have not been quite so pronounced.

The general conclusions to be drawn from these figures on the whole support the analysis with which this section began. The present depression is a combination of agricultural, industrial, commercial and financial disorganisation. But that disorganisation, which has arisen from a combination of different causes, affects agricultural production very differently from manufacturing production. The crisis which has paralysed international finance and credit, and bids fair to strangle international trade, has severely shaken manufacturing enterprise, including the production of mineral raw materials. But agricultural production, the extension of which in recent years is one of the causes of disorganisation, does not decrease though stocks accumulate. The farmer, faced with a reduction in his income, exerts every effort to increase his production in order to counteract the effect of lower prices. There are limits within which it is possible for him to do this. He must purchase or hire instruments of production and he must in the end sell his produce. The closing in of these limits will be considered in the next section, but meantime it is clear that agricultural production has been sustained in a remarkable way during the depression. This, however, is a different thing from the maintenance of agricultural purchasing power which, it will be shown later,² has declined alarmingly. It is the decline of purchasing power because of low agricultural prices which, added to the manufacturer's own troubles, and to the breakdown of international trade and

¹ Cf. monthly figures annexed to *Review of World Production, 1926 to 1931*.

² See Chapter IV.

finance, has brought about the severe contraction of industrial production.

This contraction, it should be emphasised again, is far greater than in any similar period of depression for which there are statistical records. Professor Ohlin, writing in the latter part of 1931, cited several significant estimates of the severity of the decline in industrial production during the recent depression.¹ Later information shows that, in the months since these estimates were put together, the decline has been even more severe. Thus the production of pig-iron in six important producing countries,² which declined from 1929 to the first half of 1931 by about 40 per cent, in March 1932 had declined by 64 per cent from the 1929 level. In the United States of America, the volume of industrial production, as measured by the index of the Federal Reserve Board, declined by 23 per cent between 1920 and 1921 and by 33 per cent between June 1929 and December 1930, but by December 1931 the decline was 41 per cent. The abnormal decline in world trade, which was estimated as about 40 per cent between the spring of 1929 and that of 1931, was nearer 60 per cent in the spring of 1932.³ There is ample evidence, therefore, concerning the unprecedented degree to which the industrial structure of the world has been shaken, especially during the most recent phases of the depression.

(iii) THE DEPRESSION IN AGRICULTURE.

The depression in agriculture, which is a large part of the present crisis, is almost world-wide. With the possible exception of China and Russia, there is no country where the agriculturists, despite special measures of protection, have not suffered severely from the precipitous decline in the prices of their products. There are few commodities of agricultural origin which have not fallen heavily in price. The Javanese peasant who produces rubber, cocoa and similar tropical products suffers together with the Brazilian coffee-grower, the sugar-planters of Hawaii and Cuba, the dairy-farmers of New Zealand; the meat-producers of Argentine share the difficulties of the Danubian wheat-growers.

Although the fall in the prices of agricultural products has been particularly severe and the suffering caused thereby has in many countries been intense, the productive organisation of agriculture is not disorganised in the same way as that of manufacturing, commerce and finance. The purchasing power

¹ *Course and Phases of the World Economic Depression*, pages 274 to 277. The series chosen have all been adjusted for seasonal variation.

² United Kingdom, France, Germany, Belgium, Sweden, United States.

³ See Chapter V.

of the farming communities has greatly declined, and this is a very powerful factor in creating disorganisation of the secondary processes — trade, manufacture and finance — but agricultural production is maintained and, in many cases, even increased. The table below shows this fact quite clearly :

Group Indices of Production in the World as a Whole weighted by 1930 Values.¹

(Basis : Average for 1925 to 1929 = 100.)

Group of Products	1925	1929	1930	1931 ²
Cereals	99	101	102	98
Cereals and other food-crops.	97	102	103	100
Meat	95 ²	104 ²	99 ²	...
Wine and hops	109	108	94	96
Coffee, tea, cocoa	88	120	92	106
Tobacco	99	106	109	...
Vegetable oil materials	95	107	100	105
Textiles	97	106	103	104
Rubber	80	132	125	121
Wood-pulp	86	117	113	...
Fuels	93	110	101	92
Metals	88	116	95	71
Non-metallic minerals	87	112	109	...
Chemicals (fertilisers)	88	123	111	...

The maintenance of agricultural production disclosed by these figures must, however, be considered with the available statistics of world stocks of important commodities. There has been a very great accumulation of stocks as the depression has proceeded. Some of the outstanding statistics are reproduced in the next table :

World Stocks of Important Agricultural Commodities, 1925 to 1931.

Commodity and Unit	Month	1925	1929	1930	1931
Wheat (millions of quintals)	August	114	233	220	246
Sugar (millions of quintals)	December	37 ³	57	71	87
Coffee (millions of quintals)	March	5 ³	9	16	17 ⁴
Cotton (millions of bales)	December	5,635	7,234	9,396	10,709
Rubber (thousands of metric tons)	March	—	243	367	556 ⁵

¹ See *Review of World Production, 1925 to 1931.*

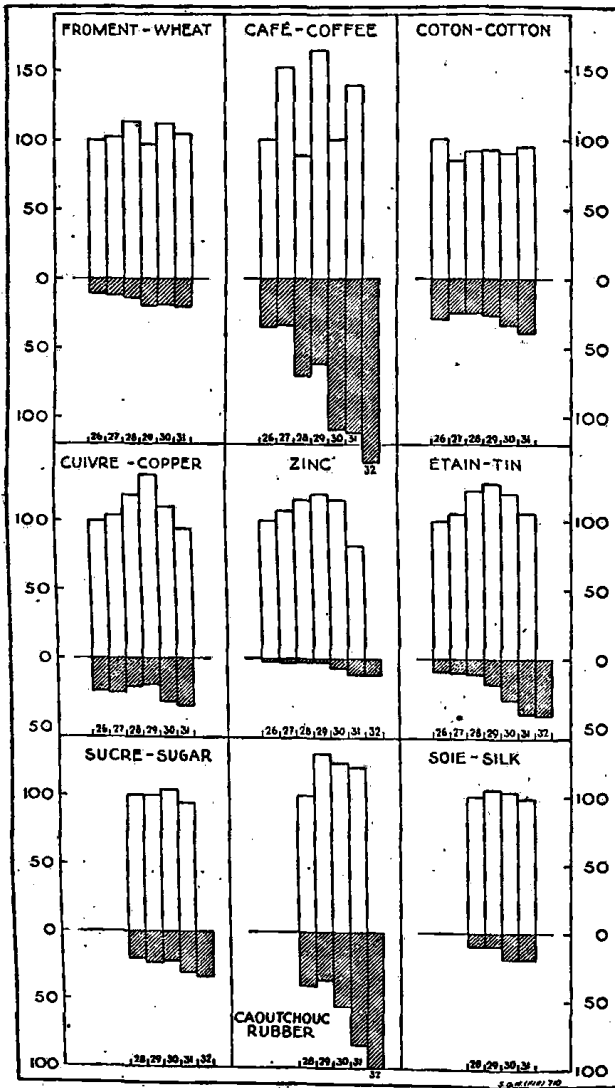
² Provisional indices, partly based on estimates.

³ Statistics for 1926.

⁴ Stocks at February 29th, 1932, were 205,000,000 quintals.

⁵ Stocks at February 29th, 1932, were 654,000 metric tons.

Production and Stocks of Staple Commodities.¹



□ Yearly production ■ Stocks

¹ All stocks are for March 31st of each year, except wheat—July 31st; cotton—December 31st; and silk—June 30th.

Sources :
 Wheat : *Wheat Studies*, Stanford University.
 Coffee, Copper, Zinc, Tin, Sugar, Rubber : *Monthly Bulletin*, London and Cambridge Economic Service.
 Cotton : *Economisch-Statistische Berichten*.
 Silk : *Statistisches Jahrbuch für das Deutsche Reich 1931*, International section.

Such very heavy stocks obviously represent a serious maladjustment of demand and supply. The stock of wheat is the largest in the history of the trade and represents nearly a fifth of the total world crop in 1930-31. The sugar stocks represent about one-third of the average yearly supply, and coffee stocks represent fifteen months' consumption at present levels.

Many factors enter into this maladjustment. There is, in the first place, some fluctuation in demand. It is difficult to summarise the conflicting tendencies at work; but, in the post-war years, it is evident that rising standards of living and changing diet habits caused important shifts in demand for agricultural products. The substitution of mechanical tractors for horses in the farming operations of many countries also disturbed both the demand for cereals and the rotation of crops in many areas. In face of the changes taking place in demand, the markets for production have been rendered rather more uncertain, but there has been no decline in the world demand for agricultural products as a whole or for such an important product as wheat. The demand for wheat may have fallen off somewhat in the United States and in certain parts of western Europe, though this is doubtful, but, with prosperity, large groups of people who formerly ate the cheaper grains began to use wheat. There is an enormous potential, but not as yet effective, demand for foodstuffs and raw materials in the Far East, and in recent years an increasing quantity of wheat has in fact been imported to China.¹ It has, however, been suggested that a decline in consumption caused by restrictive import policies and by falling purchasing power, as distinct from changing diet habits, has played an important part in the fall, for example, of wheat prices after 1930.²

On the side of production, two important factors have contributed to maintain world production and increase world stocks. The first is the revolution in agricultural technique which has been proceeding mainly in the newer farming countries, and the second is the restoration of European (including Russian) production, particularly after 1925.

There is no doubt of the enormous advances already made and of the possibilities still remaining in the application of scientific and mechanical technique to farming processes. The case of cereal-growing, and especially wheat-growing, is particularly significant. The use of the tractor and the harvester combine, the breeding of new wheats to resist drought or to mature quickly in regions likely to be visited by early frosts, the improvement of fertilisation and the control of insect and

¹ See "Wheat Studies", Food Research Institute, Stanford University, Vol. VI, No 10.

² Cf. R. R. Enfield, "The World's Wheat Situation", *Economic Journal*, December 1931.

fungoid diseases, have added large quantities of important foodstuffs to the world's production. Cane-sugar production has also been increased greatly by mechanical methods of handling and transport and particularly by plant-breeding and control of parasites. Many other examples might be cited of the increase of output, cheapening of cost, and improvement of quality which have followed upon more scientific organisation and control of the productive processes.

The disturbing effect of these improvements arises, not so much from over-production in any absolute sense of the word, but from the disorganising effect which they have upon existing economic arrangements. There is, no doubt, given the existing standards of living and food habits and the existing restrictions on freedom of trade, some measure of temporary over-production of important agricultural products. The mere existence of large surplus stocks is sufficient to indicate such a maladjustment of supply and demand. Whether that maladjustment is anything more than temporary is, however, quite another matter. It would be hazardous at the present moment to conclude that widespread curtailment of production was essential to relief of the depression in agriculture.

It is clear, however, that there have been very large shifts in the chief areas of production and that these are disturbing causes in the crisis. A comparison of the production, and still more of the exports, of wheat in the pre-war and post-war periods is illuminating in this respect.

Net Wheat Exports Pre-War and Post-War.¹

Quintals (000's)	Percentage of world exports	
(Annual average, 1909 to 1913.)		
U.S.S.R.	41,174	24.1
Argentine	24,249	14.2
Canada	20,152	11.8
Danubian countries	19,056	11.2
U.S.A.	14,296	8.4
India	13,176	7.7
Australia	11,430	6.7
	(Annual average, 1926 to 1930.)	
Canada	70,051	37.1
Argentine	40,764	21.6
U.S.A.	27,334	14.5
Australia	17,459	9.2
U.S.S.R.	8,149	4.3
Danubian countries	5,720	3.0

¹ See *Annuaire international de Statistique agricole, 1930-31*, Rome.

The large increase in the export surplus of those countries which are able most easily to apply the new methods of production is very clear. But the renewal of strong competition from the European producing countries was very marked also after 1928. Between 1928 and 1930, the share of Europe in the world exports of wheat rose from 4 to 25 per cent.¹

A substantial part of this increase in European exports was due to the re-emergence of the Union of Soviet Socialist Republics as an exporter of wheat on a considerable scale. Before the war, the Russian export surplus was larger than that from any other country. Even in 1928 and 1929, the Soviet Government found it necessary to import wheat. In 1930, however, and in 1931, large quantities were exported under the Five-Year Plan.²

There is a substantial difference between these Russian exports and those from other European wheat-producing countries on the one hand and the export surpluses of the new producing countries on the other. Pressure of necessity forces the European exporters to sell, but, during the early stages of the depression, the producers in other countries were able to hold supplies off the markets for a time. As, one after another, the price control schemes broke down, successive accumulations of stocks were dumped on an already demoralised market. The fall in prices and the persistent low level which has prevailed since 1929 are not, therefore, to be attributed to any one factor. They are the result of the combined pressure of increased supplies from many countries upon a world-demand which is restricted by trade barriers and diminished by lowered purchasing power.

In the case of certain products, such as sugar and rubber, part of the production of which is dependent upon large-scale capitalist organisation, there enter other factors such as the time-lag before investment becomes productive. It takes about seven years for a rubber tree to mature and it is probable that still greater production of this commodity is to be expected as trees come into profit which were planted in the boom. Sugar production also calls for capital investment and cannot quickly be restricted. Moreover, the greatly increased production of cane sugar in recent years has encountered renewed competition from beet-sugar in Europe.

Credit expansion in the years 1925 to 1929 obviously played a considerable rôle both in promoting the new methods of production in such countries as the United States of America,

¹ The increase was equally marked in other cereals. — *e.g.*, in rye, from 44 to 96 per cent; in barley, from 21 to 82 per cent; in oats, from 38 to 60 per cent; in maize, from 7 to 26 per cent. (See *Review of World Trade, 1930*, page 37.)

² The quantities of wheat exported from the Union of Soviet Socialist Republics in recent years have been: in 1928, 33,283 quintals; in 1929, 50 quintals; and, in 1930, 25,309,350 quintals.

Canada, the Argentine, Australia and the Soviet Union, and also in restoring the production of the European countries. Cheap and easy credit made possible a rapid extension of the use of the new agricultural machinery, and also facilitated the various attempts at price-controls. At the same time, a high general level of purchasing power was maintained, the price of agricultural products remained high and European production was tempted again into world markets.

The subsequent breakdown of the credit inflation and the fall in prices which resulted from it have been aggravated by the almost complete collapse of international markets for many of the most important foodstuffs. In the next chapter, a table is given showing how widely the domestic prices of wheat in different countries now vary. Tariffs, quota systems, contingents, clearing arrangements, milling regulations, have destroyed free competition in the international market and have substituted for it a series of sheltered but inevitably weak producers for domestic markets. Such measures are encouraging production where it is costly and discouraging it where it is more efficient. If it is only by such measures as paralyse world trade that temporary shelter may be given to the threatened producers, such shelter may prove to be dearly bought in the long run.

There is, in the spring of 1932, little sign of significant restrictions of acreage under cultivation.¹ Marked reductions in winter wheat acreage in the United States have been followed by favourable spring sowings, and from Canada at least a large export surplus is expected.² The harvest prospects in the Soviet Union and in other exporting countries are not yet known. There is, however, significant difficulty in providing mechanical equipment in many of the more efficient areas ; and also in the provision of fertilisers for the world as a whole. This phenomenon, to be noted in many individual countries, is manifested also in the production of the chemical industry, which fell by 10 per cent in 1930 and by a further 25 per cent in 1931. It would be ironical if the restriction of production ultimately induced by the depression were carried to the point where not only existing stocks disappeared, but production was curtailed especially in the areas of cheaper production.

(iv) THE DECLINE IN INDUSTRIAL PRODUCTION.

The statistical information that is available concerning the production of raw materials as distinct from foodstuffs, and particularly of those raw materials used for the production of

¹ Cf. *Monthly Bulletin of Agricultural and Commercial Statistics*, April 1932.

² See *The Times*, London, June 7th, 1932.

investment goods, supports the argument advanced in the first section of this chapter that the disorganisation of production has been greater in the manufacturing industries than in agriculture. This information is in accord also with the trend of the national index-numbers of production and with such material as is available concerning the position of particular important manufacturing industries.

When the whole period 1925 to 1932 is considered, it becomes evident that, by the beginning of 1929, the disequilibria inherent in the reconstruction boom had become apparent. The table cited below offers evidence of this.

Index-Numbers of Raw Material Production, weighted by 1930 Values.

(Basis : Average for 1925 to 1929 = 100.)

Continental Groups	1925	1929	1930	1931 ¹
Europe, excluding U.S.S.R.	90	117	102	91
Europe, including U.S.S.R.	88	117	107	99
North America	94	108	93	81
Latin America	92	111	105	—
Africa	97	110	108	96
Asia (excluding Asiatic Russia) . . .	94	107	109	97
Oceania	93	102	97	95
World	92	111	101	91

It is significant that the production of raw materials in the years 1925 to 1929, as measured in this table, increased fastest in Europe and Latin America, where American loans were extended most freely. The development was most marked in Europe, where, even when the Soviet Union is excluded from consideration, there was a cumulative annual increase of 4 per cent. The subsequent decline in production has been greatest in these areas and in the United States itself, where the inflation was most pronounced and where there was a very marked expansion of production between 1913 and 1925.

Even the severe measure of decline which is revealed in the production of raw materials does not reveal the full extent of the industrial depression. As in the case of agricultural products, there have been marked accumulations of stocks, and, in many cases, price-control schemes which have, after sustaining prices for a short time, broken down and released accumulated stocks on an already disorganised market. Many important mineral

¹ Provisional indices.

raw materials — copper, lead, zinc, tin, aluminium — are controlled by more or less strongly organised cartels. The stocks of non-ferrous metals have increased very greatly since the depression began.

*Stocks of Non-Ferrous Metals.*¹
(Metric tons, 000's.)

	April 1st	Copper	Lead	Tin	Zinc
1925	401	...	20	16
1929	278	...	27	36
1930	487	45	43	91
1931	518	132	61	142
1932	165	62	140

In the *Review of World Production, 1925 to 1931*, from which these and the other statistics cited in this chapter are drawn, an attempt is made to estimate the degree of decline in industrial production. It is obvious that this must be greater than the decline in raw material production if only because stocks of raw materials have accumulated in such great quantities. A combination of the national indices of production compiled in the main industrial countries, shows that production as a whole fell by about 25 per cent between 1929 and 1931. Since the production of foodstuffs in the world was practically stable, it is obvious that the decline in raw materials and in manufacturing production must have been very great. If an index of manufacturing production alone could be obtained, it would show a greater decline than 25 per cent. Moreover, the decline has been very rapid in the latter part of 1931, so that the annual average understates the decline.

Conditions have varied from country to country and from industry to industry. The publication referred to above briefly surveys the main facts first by countries and then by industries. The only country which records a marked and cumulative increase in industrial production during the depression is the Union of Soviet Socialist Republics. The available statistics² show an increase in the total value of industrial production of 30 per cent in 1930 (at constant prices) and of approximately 22 per cent in 1931. This increase is of course calculated from a comparatively small base, so that it is hardly likely to be fully maintained. But it represents a very substantial and significant change in the Soviet Union's relation to the outside world. This is evident from the share of the Union of Soviet

¹ See *Review of World Production, 1925 to 1931*.

² Institut für Konjunkturforschung, Berlin.

Socialist Republics in the world production of industrial raw materials, which rose from 3.7 per cent in 1925 to 7.9 per cent. in 1931. The conditions under which that increase has been attained are, however, unique. The index of production is admittedly not an indication of the goods made available for consumption by the people. A sustained effort is being made to equip the Union of Soviet Socialist Republics with heavy industries and the energies of the whole people are bent to that end, rather than to the satisfaction of individual wants. This disciplined effort makes Soviet Russia a world apart, whose experiences have at the present time little relation to the situation in other countries.

The heaviest declines in manufacturing production have taken place precisely in those countries — the United States of America and Canada — where credit expansion was most pronounced in the years 1925 to 1929, but was followed by deflation in 1929-1932, and in countries like Germany and Poland, where there was a rapid recovery in 1925 to 1929 accompanied by a large volume of foreign borrowing. The most recent monthly indices of production available in those countries at the moment of writing show the following declines as compared with the corresponding month in 1929 :

	Percentage
United States (February)	41.5
Canada (February)	36.6
Germany (March)	44.1
Poland (February)	48.5

There were other countries, notably France and Sweden, which maintained a high level of industrial activity until well on in 1930 ; but as the table cited earlier in this chapter shows, all of these countries were suffering quite heavily from the depression in 1931 and 1932. Japan showed a spurt of production in the textile industry in the second half of 1931 and those countries which abandoned the gold standard in the third quarter of the year were able at least temporarily to check and even reverse the decline in production. Statistics are available for Sweden which show a temporary stimulus to the export industries, succeeded by an improvement in the industries catering for the home market.

(1925 to 1930 = 100.)

	1931					1932			
	Aug.	Sept.	Oct.	Nov.	Dec.	Jan.	Febr.	March	April
Home-Market industries	98	99	97	94	104	98	102	100	104
Export industries	83	88	91	94	98	83	94	83	77

Perhaps the most significant of these figures, however, are those which show how export trade slackened in the early months of 1932. This slackening is primarily due to the progressive closing of export markets by the various measures of trade restriction imposed in those months. The statistics cited above for Sweden may be paralleled by those which reflect the check to exports from the United Kingdom. In the same way, the later falling off of Swedish production for the export market finds its counterpart in the tendency for British unemployment figures to increase again in the spring of 1932.

The statistics which show the decline in production of the more important industries reveal a wide range of variation, as the following roughly comparable statistics for Germany and the United States of America will show.

Percentage Decline in the Production of Various Classes of Goods from 1928 (Average) to End of 1931.

GERMANY.			
Producers' Goods		Consumers' Goods	
Timber	— 27	Foodstuffs	— 9
Iron and steel (rolling-mill products)	— 43	Footwear	— 19
Non-ferrous metals	— 51	Paper	— 23
Cement	— 54	Textiles	— 32
Machines	— 58	Passenger cars	— 39
Steel	— 61	Clocks	— 41
Iron	— 64	Porcelain	— 58
Lorries	— 65	Pianos	— 81
		Motor-cycles	— 85

UNITED STATES OF AMERICA.			
Producers' Goods		Consumers' Goods	
Electrical goods ¹	— 43	Silk consumption	+ 9
Cement (Portland)	— 43	Foodstuffs	— 5
Commercial motor vehicles	— 52	Gloves	— 5
Electric motors ¹	— 53	Tobacco products	— 10
Woodworking machines	— 72	Cotton textiles	— 20
Machine tools	— 69	Books sold	— 20
Steel castings	— 73	Household furniture	— 150
Foundry equipment	— 82	Boots and shoes	— 26
Locomotives ²	— 90	Vacuum cleaners	— 38
		Baths	— 72
		Passenger cars	— 79
		Enamelled ware	— 83

¹ Values.

² Decline from average 1927 to 1929.

Broadly speaking, producers' goods have declined further than consumers' goods, and, in both categories, the more durable products have fared the worst. There is evidence indeed of a sharp decline in the standard of living in both countries, a decline expressed in the diminution of demand for the more expensive articles of personal and household equipment. This development supports the analysis of the boom which was made in an earlier chapter¹.

The heavy fall in production of those commodities which are primarily classified as investment goods is clearly demonstrated also in the case of raw materials, and particularly metals. The *Review of World Production 1925 to 1931* cites further evidence from Sweden, Poland, the United Kingdom and the United States of America, supporting the conclusion that, in all these cases, the production of investment goods fluctuated more than that of consumption goods. Moreover, the rate of decline has accelerated notably in recent months as the following table shows.

The alarming significance of this table is only too clear. The volume of production of investment goods in the United States, Germany and Poland has fallen very heavily indeed in recent months.

The only country where the production of investment goods has risen faster than that of consumers' goods during the depression is the Union of Soviet Socialist Republics. The index of the former (based on the average 1926 to 1929 as 100) rose from 140 in 1929 to 249 in 1931, while the index of consumers' goods rose from 133 to 187. At the same time, the Russian imports of capital goods have increased. Imports of metals, metallurgical products, electrical machinery and apparatus represented 31.4 per cent of the total imports in 1926-27, but, in the first six months of 1931, such imports amounted to 73.7 per cent of the total. This large demand for capital equipment has naturally affected production in certain other countries, particularly Germany.

It was shown in the preceding section of this chapter that the production of agricultural foodstuffs and raw materials has, up till the present, been relatively well sustained. Although large stocks are being accumulated, there is reason to believe that production at present exceeds consuming capacity. Prices of agricultural products are very low.

On the other hand, the production of capital equipment, except in the case of the Union of Soviet Socialist Republics, has fallen to levels which are obviously below the needs of the

¹ See Chapter II, section (i).

Indices of Production of Investment and Consumers' Goods.
(1925 to 1929 = 100.)

Country	Grouping	1929				1930				1931				1932
		I	II	III	IV	I	II	III	IV	I	II	III	IV	I
Germany :	Investment goods	105	125	119	109	100	93	84	78	72	75	67	56	46
	Consumers' goods	108	107	102	106	103	103	94	91	86	96	90	92	86
Poland ..	Investment goods	123	127	120	117	107	96	96	89	77	76	76	63	48
	Consumers' goods	122	109	104	103	92	90	92	91	87	88	81	73	68
Sweden ..	Investment goods	114	113	116	118	122	109	106	99	97	86	86	94	87
	Consumers' goods	105	108	104	103	113	103	99	102	¹ (79)	102	109	105	110
United Kingdom. (1924, 27-29 = 100)	Investment goods	105	111	107	107	108	102	93	85	83	80	73	77	78
	Consumers' goods	99	102	98	101	94	90	87	89	85	86	87	95	93
U.S.A. ..	Investment goods	110	124	124	94	96	91	79	64	65	59	48	41	35
	Consumers' goods	104	107	106	99	95	89	85	87	88	91	93	86	83

¹ Extensive labour conflict in the textile industry.

world, but prices of these goods remain relatively high.¹ This is obviously one of the chief obstacles to recovery in the present depression. Until the costs of production in the capital equipment industries, which are in most cases strongly controlled, can be so reduced as to make possible expanded production, lower prices and increased profits, these basic industries whose products are essential to business expansion generally, will remain in a depressed condition. As long as their products remain expensive it will be difficult to evoke a larger demand for them. Business enterprise depends upon the expectation of profits and, as long as capital equipment remains expensive, the prospects of business expansion are limited. Recovery in the output of the industries producing investment goods therefore will be a sign of renewed business expansion, but that recovery cannot come until the disparity which at present exists between the prices of consumers' goods and those of investment goods is remedied, either by a rise in the former or by a fall in the latter consequent upon lowered costs of production.

(v) INDUSTRIAL PROGRESS IN THE DEPRESSION.

It would be obviously impossible to attempt in a short space any systematic survey of the fortunes of all important industries during the depression. The *Review of World Production, 1925 to 1931*, contains some brief notes upon the situation of certain principal industries; but even those fuller notes and the statistical appendices by which they are supported can only be fragmentary. In this section, all that can be attempted is the raising of certain broad questions relating to the effect of the depression upon industrial progress.

It should first be said that the rapid development of new technical methods and the growth of new industries, together with the spread of industrial organisation to new countries, was one of the structural changes which tended to create an unstable situation in the years before the depression. It is true that such changes are always in progress and that they seldom cause such violent paroxysms of readjustment as the world has recently witnessed. But, in the present situation, two important elements have to be taken into account. The first is the increased pace at which the changes took place, partly as a result of mechanical invention during the war period and partly as a result of credit inflation during the boom which preceded the present depression. The second lies in the less flexible organisation of post-war economic life, as a result of which readjustment to meet changing

¹ See Chapter IV.

conditions of production was rendered much more difficult. All the apparatus of economic nationalism and governmental intervention, cartels and industrial organisations, and banking assistance to threatened industries, interposed obstacles to the elimination of less effective industrial methods.

The credit expansion which was so marked in the latter part of the first post-war decade supported first a high level of consumption and then an investment boom with the result that an expansion of the new, and a maintenance of the old, industries finally culminated in a situation where capital equipment outran consumers' demand. Examples of this might be drawn from many industries. Cereal-growing has already been mentioned; the textile industries offer another example, not only of new products and new methods coming into vogue, but also of new areas of production being developed without corresponding liquidation of the older areas. The coal industry in many countries has been the subject of governmental intervention to save it from the full consequences of the increased competition of other fuels and sources of power. Competition between the railways and newer forms of road transport is acute in most countries.

It seems clear that many unsound elements crept into the expansion of business enterprise during the boom period and that the process of contraction during the depression has been especially severe in certain of the newer industries. This is true, for example, of the motor-car industry. The monthly production of cars in the United States in 1931 averaged less than 50 per cent of the comparable figures in 1929 and fell much lower in the first quarter of 1932. The recession in Canada was even more marked, production in the first quarter of 1932 being only 18 per cent of that for the first quarter of 1929. German production also fell off very heavily, but the fall in France and the United Kingdom was much less.

Many factors enter into this situation. Recession has been greatest where there was the most marked credit inflation. It is evident also that the technical methods of mass production which formed the chief advantage of the American industry are now being utilised in other countries. Behind tariff barriers domestic markets in these countries are slowly being expanded. The American industry, faced with a sudden contraction of purchasing power in a market already close to saturation point, is also faced with export difficulties arising from more effective foreign competition as well as from tariffs and other trade restrictions.

The failure of demand from the motor-car industry and also from constructional building activities lies behind the plight of

the iron and steel industry, especially in the United States. This is a typical and important example of the way in which an unduly extended consumer's demand, especially for products of durable consumption, was responsible in the boom period for an over-expansion of capital equipment in certain leading industries. A large part of the recession in production has come in the industries which cater for the new ranges of demand made possible by higher standards of living. The recoil of these standards from the levels reached during the boom has been very marked.

This, however, is quite consistent with the much more important fact that, broadly speaking, the new industries, new methods and new areas of production continue to win their way in competition with their older rivals. It is obvious that, when purchasing power declines, motor-car production is likely to be curtailed more than the production of foodstuffs and clothing, but, if the motor-car industry is badly hit, it is mainly on the passenger-car side of the business. Motor transport continues to make headway against the railways of most countries.

There are many examples which might be cited of the continuing advantage, even during the depression, of new products, new methods and new areas of production. Shipbuilding has suffered heavily. In March 1932, the total tonnage under construction was 1,298,000 as against 3,266,000 in March 1930, and even this decline does not fully represent the position since work was suspended or slowed down on many ships. The contraction was very heavy in the United Kingdom, Germany, Japan, the Netherlands and Denmark, but less pronounced in France, the United States and Sweden, while Italy recorded an uninterrupted expansion throughout the depression. It is of interest also to observe that motor-ships, which in 1925 accounted for 38.5 per cent of the tonnage launched, in 1929 accounted for 45 and in 1931 for 57 per cent. Of the total steam tonnage launched in 1931, approximately 79 per cent refers to ships fitted for burning oil fuel, the tonnage depending exclusively on coal for propulsion being less than 10 per cent of the world output in that year. This is clear evidence of rapid technical changes being accentuated during the depression.

In the textile industries there is much evidence of growth in the newer areas of production, which, in addition to other advantages, are able to use the most modern equipment. Thus, in India and in China, cotton manufacture expanded throughout the depression.¹

¹ Full statistical summaries of these and other industries cited are given in the appendices of the *Review of World Production, 1925 to 1931*.

It seems clear also that there has been a strong trend in favour, not only of artificial silk and silk fabrics, but also of the finer qualities of cotton and wool, and that the world output of hosiery and knitted goods has expanded greatly. The output both of natural silk and of artificial silk continues to increase, but with important shifts of production. Artificial silk indeed is one of the very few industries that has been able both to expand its production and to maintain its prices during the depression. Prices, which fell, according to Italian quotations, by 60 per cent between 1925 and 1929, have not fallen more than about 7 per cent between 1929 and the beginning of 1932. As in the case of natural silk, production tends to shift to the United States and Japan.

The production of electrical energy, which increased very fast between 1925 and 1929, has been maintained during the depression. The advance was particularly great in the Union of Soviet Socialist Republics, Finland, New Zealand, Netherlands, Belgium and Japan, but this form of power is being developed very rapidly in almost every country and with it new engineering industries and new technical methods in the older industries are being sustained.

The general impression gained from the survey of manufacturing production during the depression from which the above examples are cited, is one of continuing technical progress and increasing competition from the newer methods. The more efficient methods tend to win the battle during a period of depression, but the vested interests of the older productive organisation are very strong, and many obstacles are put in the way of readjustment to the new technical situation. Such obstacles, expressed, not only through governmental, but also through industrial and banking policy, form a large part of the background of the present depression and are no less important in delaying the readjustment of the relation between prices and costs of production which is necessary to recovery.

Chapter IV. THE MOVEMENT OF PRICES.

(i) ELEMENTS OF INSTABILITY BEFORE 1929.

A previous publication of the Economic Intelligence Service of the League of Nations has reviewed the movements in the general level of wholesale prices during the years which preceded the present depression.¹ The information gathered in that publication is sufficient to show that there was, in the world as a whole, little uniformity in the movement of wholesale price indices in different countries during the years 1922-1929. Even when the influence of various degrees of currency depreciation is removed by converting all the indices to levels corresponding with the gold parities of the different currencies, there still remains a wide range of variation in the national price-levels. Compared with 1913 or 1914 as base = 100, the wholesale price index-numbers of thirty-one different countries stood in 1928 at levels ranging from 165 (Australia) to 119 (Chile). Moreover, the movement of these indices in the years 1922-1929 was not uniform either from year to year or over the whole period.

After the restoration of the gold standard by many countries in the years following 1924-25, there was a tendency for the various national price-levels to be brought into equilibrium; but this involved the necessity for adjustments of certain national price-systems, adjustments, moreover, to an international equilibrium that was constantly changing as more countries stabilised their currencies and as world production and trade recovered. The general level of prices in Britain, for example, moved steadily downward after 1924, while the level in the United States remained relatively stable, with only a slight falling tendency. Between

¹ *The Course and Phases of the World Economic Depression*, pages 87-96.

1924 and 1929, the Board of Trade index of wholesale prices in Great Britain fell by 18 per cent, the United States Bureau of Labor Statistics index by 3 per cent; the German official index remained very steady; and the French index remained steady also after the stabilisation of the franc in 1927-28. The Italian index fell by 26 per cent between 1926 and 1929, and the Japanese by 7 per cent, while the Australian index fell by only 2 per cent in the same years.

The return to the gold standard by Germany (1924), Great Britain (1925), Italy (1926), France (1927-28), and many other countries in this period had made possible the hope that, after the necessary adjustments of the domestic price-levels had taken place, international equilibrium would be maintained by the normal operation of the foreign exchanges. But there was very great difficulty in choosing the levels at which to reattach the depreciated currencies to gold. No level which might have been chosen in any particular case exactly fitted all the domestic and external requirements, and many of the factors that had to be considered, such, for example, as the repatriation of capital, were incapable of precise estimation. In retrospect, it is clear enough that Great Britain and Italy returned to gold at parities which necessitated a large and difficult measure of internal deflation, while France and Belgium stabilised at levels which encouraged the return of foreign balances and allowed domestic (retail) prices to rise.

It is evident, therefore, that, while adjustment of internal to external purchasing power was proceeding in many countries after 1925, the world's currencies had not been brought into stable equilibrium when the crisis developed in 1929. This fact must be reckoned as a major element of instability in the pre-depression years.

In addition to this international disequilibrium, however, there were many important elements of instability in the price-structure, even of those countries where the index-number of wholesale prices appeared to be relatively steady. Such relative stability of the average level of wholesale prices, in fact, concealed weaknesses within the price-structure which were at least partly responsible for the severity of the decline in prices which followed after 1929. Some reference has already been made to the general economic factors of instability in the first post-war decade.¹ The analysis which follows of the effects of a rapid credit expansion in the years 1925-1929 must be regarded as an added, but not the sole, cause of price instability. Indeed, as has already been shown (Chapter I, section (viii)), the credit

¹ See Chapter I.

expansion itself was due, in part, to the attempt at facilitating the restoration of Europe and, in particular, to the provision of new loans to "bridge the gap in the balance of payments".

The level of wholesale prices was more stable in the United States of America than in most other countries. In 1923, the Bureau of Labor Statistics wholesale price index stood at 100.6 (1926 = 100). It rose to 103.5 in 1925 and fell to 95.3 in 1929. The year-to-year changes in this whole period did not exceed 5 per cent in either direction, though there was a somewhat wider range of movement when the monthly figures are considered. Retail prices in the United States showed an even smaller variation; but wages increased steadily over the whole period. The index-number of wholesale prices of commodities does not, however, cover the whole price-structure, and there was much evidence, particularly in the years 1927-1929, of a considerable inflation of security and real estate prices caused by the credit expansion discussed in an earlier chapter of this *Survey*.¹

Moreover, this marked expansion of credit, which followed the cheap money policy of the Federal Reserve Banks in 1927, had very different effects upon different groups of commodity prices.

When the situation of all the gold-standard countries is taken into account, it is probable that the average world-movement of gold prices in the years 1925-1929 was substantially downward. But productivity was increasing fast, and prices would probably have fallen more markedly if there had not been an expansion of credit. The stability of the average level of wholesale prices in such circumstances was favourable to business expansion and higher profits.

Even though the average level of wholesale prices remained relatively stable, there was an upward pressure upon many price-groups. The security and real estate speculation already mentioned yielded paper profits the expenditure of which helped to maintain the demand for, and therefore the prices of, many commodities. Low interest rates also made it possible to finance valorisation schemes, controls, pools, etc., especially for agricultural products which were kept at price levels which it proved impossible to support after the cheap credit was no longer available. Behind the shelter of these schemes there was a large extension of production which later proved a very depressing influence on prices. Finally, cheap credit facilitated the issue of loans by which many countries outside the United States maintained or buttressed their domestic price-levels and so postponed the adjustments of costs of production which were

¹ See Chapter II, section (i).

necessary if they were to remain on the gold standard. Each of these three inflationary effects of the credit expansion in the United States — security speculation, valorisation schemes and large foreign issues — contributed to the maintenance of consumer's demand.

Within the stable average, there was a marked rise of agricultural relatively to non-agricultural prices, accompanied by increased production. Agriculture shared in this period the technical progress which was characteristic of industry as a whole, and there is no reason to believe that the increased supply was produced at greater cost. Cheap and easy credit not only facilitated the holding of stocks in various price-control schemes, but made possible the utilisation on a large scale of mechanical methods of production. Technical progress is always conditioned by the cost of the capital outlay involved, and it is probable that a large part of the increased agricultural production of the period 1926-1929 was due primarily to cheap credit facilitating the use of tractors and similar agricultural machinery.

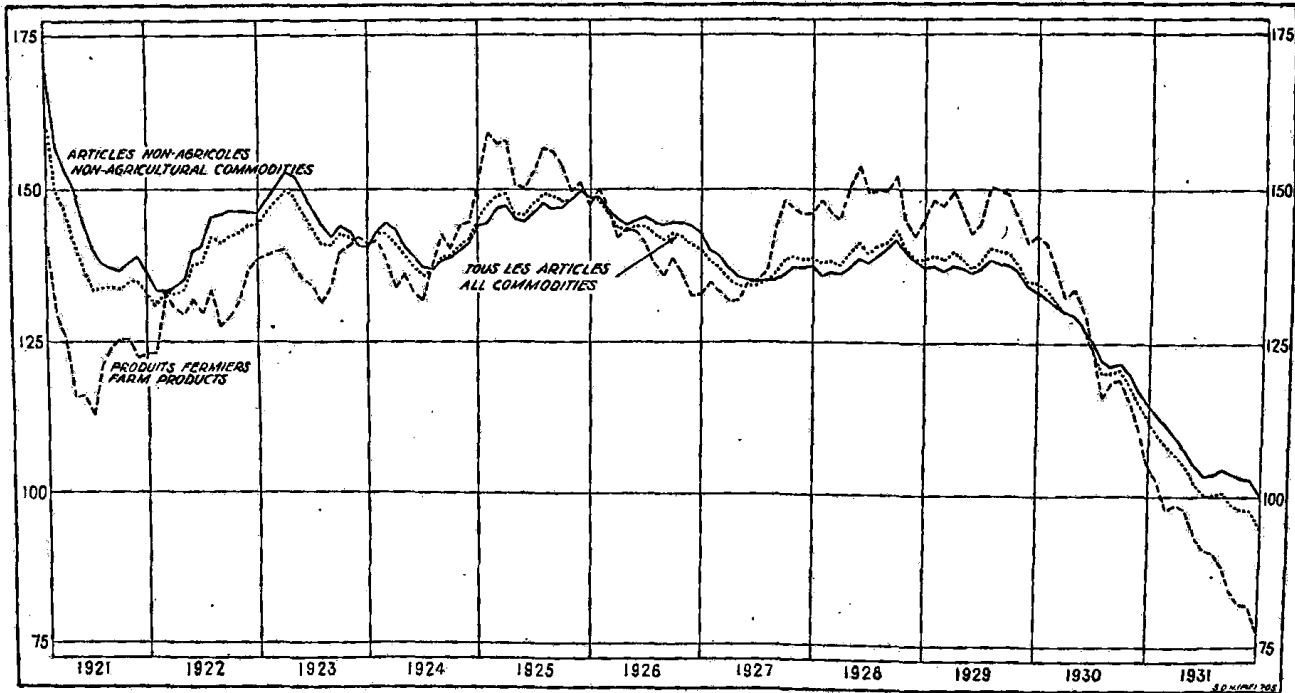
The sales of tractors and harvesting combines, especially in the United States, Canada, the Argentine and Australia, increased remarkably in this period, and there was heavier investment in fertilisers also. There was, therefore, a marked increase in agricultural production in the years of cheap credit.

The demand for agricultural products, on the other hand, tended to decrease. Rising standards of living shifted the demand from the simple basic products, such as cereals, to more elaborate and highly-priced products. In such circumstances, a downward trend of agricultural prices might reasonably have been expected, and some curtailment of production might have been looked for. The marked rise of agricultural prices shown on the accompanying diagram, together with the expansion of production that took place, gives evidence of an unstable price situation. When the cheap credit that had promoted this development was no longer available, the stocks accumulated in excess of demand were a depressing factor in the price decline.

The rise in agricultural prices was caused primarily by the influence of cheap credit upon the price of agricultural raw materials as distinct from finished products. A similar influence was exerted upon other raw-material prices, particularly those of certain mineral products. Just as the production of sugar, wheat, cotton and other agricultural products was buttressed and their prices maintained, so copper, nickel, certain types of building materials and similar products were controlled and their production extended. The United States Bureau of Labor Statistics index-numbers of the wholesale prices of raw materials and finished products show a distinct tendency for the former

Wholesale Price Indices of Agricultural and Non-Agricultural Products in the United States, 1921-1932.

(Base 1913 = 100.)



to rise relatively to the latter in the period of cheap credit from the middle of 1927 to the end of 1928.

Moreover, the influence of this cheap credit policy extended to overseas countries, both by facilitating the issue of foreign loans and also by reason of the tendency of raw-material prices to rise. It is significant that the barter terms of trade (the relation of export to import prices) became more favourable to the raw-material exporting countries at this time.¹

Particular importance attaches to the irregularity of capital movements in the whole period 1925-1932. Very heavy borrowing in the years 1925-1928 was succeeded by a period of growing stringency (1928-1929) and then by an almost complete stoppage and even reversal of capital exports from the creditor countries. These fluctuations of foreign investment, affecting not only prices but the organisation of production, though greatly influenced by credit policy, were dependent also upon general economic, non-monetary conditions. The decline in prices since 1929 is not to be explained, therefore, wholly in terms of monetary and credit causes. On the contrary, "the fundamental causes which have brought about the decline of the wholesale price-level are obviously those which made for general instability and for sudden and considerable changes in the volume of investment, international capital movements, the exchange between manufacturing countries and other countries".²

When pressure was brought by the Federal Reserve Banks to check further credit expansion from the early part of 1929 onwards, the effect of higher interest rates was not felt immediately by the security and real estate markets; but its effect upon agricultural prices, and upon raw-material prices, as well as upon foreign lending was evident in the early months of 1929. The resistance to lower price-levels was broken, accumulated stocks were liberated at first slowly, but, after the breakdown in security speculation in October 1929 created credit stringency, the selling pressure became more pronounced.

Control schemes broke down and prices slumped. The debtor countries also, deprived of the capital imports upon which they had relied, were forced to restrict credit. Increased quantities of their produce were thrown on world markets, while imports were restricted in order to provide a balance of payments for the service of debt previously contracted. The reduction of their capital expenditure also cut down their demand for the products of industrialised countries. Those industrialised countries which, like Germany, were also debtors, reduced their imports of raw

¹ Cf. Chapter VI and *Review of World Trade*, 1931, page 52.

² *Course and Phases of the World Economic Depression*, page 226.

materials and consumed their stocks, thus further demoralising the markets.

Despite the comparative measure of stability of the average level of wholesale prices in the years 1922-1929, therefore, it is clear that, in the years immediately preceding the depression, especially in 1927-1929, credit expansion, superimposed upon an unstable economic and political situation, had created a dangerously unbalanced price-structure. The pressure upon price-control schemes, and upon the debtor countries, when credit became more expensive, caused prices to fall more sharply, at least from the beginning of 1929. When the boom burst in October 1929 that fall, as the next section will show, rapidly took on catastrophic proportions.

(ii) THE COLLAPSE OF PRICES, 1929-1932.

The collapse since the latter part of 1929, not only of the average level of wholesale prices, but of the whole price-structure, has been the most alarming manifestation of economic disorganisation in the present depression. It is so far-reaching and complete that it is unlikely to have been produced by any single cause. The variety and contradictory nature of the explanations offered, even in expert circles, leads in itself to a suspicion that the causes are complex and not fully understood. It is not only the monetary mechanism but the whole economic organisation of the world that has been affected, and it is unlikely that any single weakness would have caused such a general collapse.

In even the briefest recital and analysis of price-movements in 1929-1932, therefore, consideration must be given to many other phenomena besides the outstanding fact of an unprecedented decline in the average levels of commodity prices. The price-structure of the modern world, kept in international equilibrium by the operation of the gold standard, was a very complex and delicate creation, comparable with the nervous system of the human body. By its reactions to the stimuli of changing economic conditions, the body economic was maintained in a healthy condition. Like the nervous system, it was capable of becoming deranged. On the other hand, its efficiency was hampered whenever abnormal local happenings either distorted or thwarted its reactions. An accumulation of such strains might throw the whole system into disorder.

As succeeding sections of this chapter will show, not only has the delicately balanced international equilibrium maintained by the various national price-structures been temporarily destroyed, but a whole series of disequilibria have been set up between wholesale and retail prices, the prices of raw materials

and of finished manufactures, of producers' goods and consumers' goods — to mention only a few. It is no easy task to construct once again an international system which is built up of so many interlocking and shifting relations. This destruction of the balanced relationships in the price-system is important, not only because of the inconvenience and hardship it causes by upsetting the organisation of economic life, but also because the disequilibria set up tend to act as a block to recovery.

The report of the Gold Delegation, published by the League of Nations in June 1932,¹ sets out clearly the disturbance of economic order occasioned by such a rapid fall in prices as the world experienced in the years 1929-1932. The diagram which follows may supplement this description by showing how difficult a situation has been created by the uneven incidence of falling prices. If the index-number of general prices² as calculated for the United States be taken as a rough indication of the effect of the depression on the price-structure as a whole, the dispersion of the various index-numbers around that average gives an indication of the degree to which relationships existing in 1929 have since been dislocated. It is significant that the heaviest fall has been in security prices, which are based mainly upon estimates of business profit and which therefore register the inducement to business activity. Their low level indicates the paralysis of productive activity that has resulted from the depression.

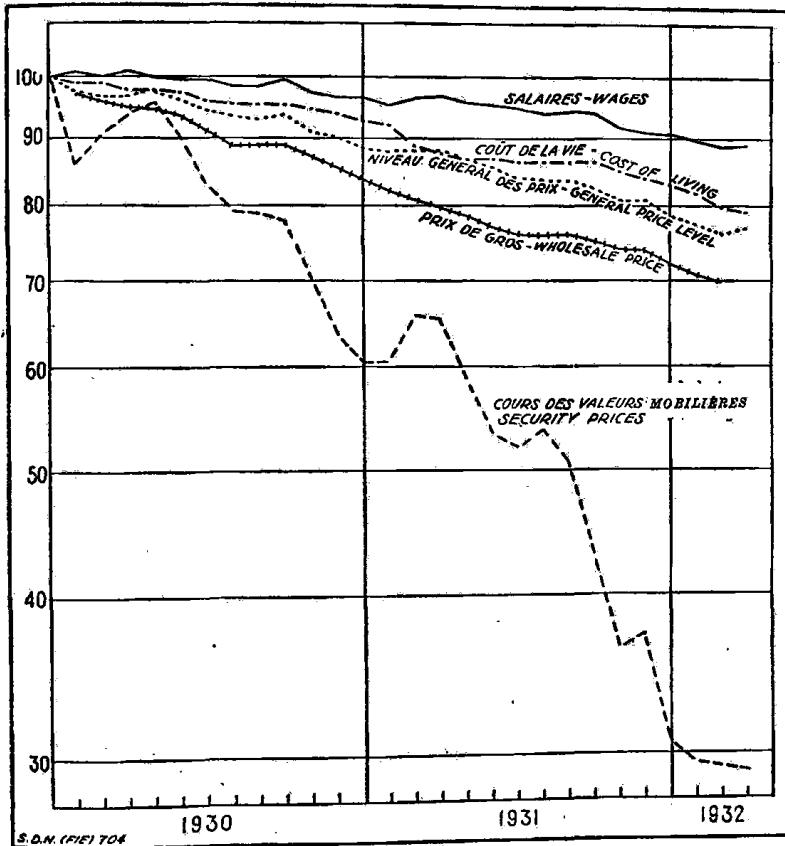
The divergent movements of wholesale prices, wages, and the cost of living, as disclosed above, are also significant, since they set up strains which lead to class disputes and industrial strife. The elements which enter into the cost of living, and therefore influence wage rates, are determined only in part by the larger economic forces which govern wholesale prices. House-rent, inland transport charges, the cost of essential services, such as the provision of water and electricity, are not as sensitive to the competitive forces of changing business conditions as are the wholesale prices of most commodities. The problem of keeping such slow-moving, inelastic prices in equilibrium with the movements of commodity prices affected by every change in sensitive international markets involves a reconciliation of national stability with international adjustment. Failure to achieve this reconciliation in the post-war period has temporarily disorganised the international price-system and wrecked the international monetary mechanism.

¹ *Report of the Gold Delegation of the Financial Committee* (document C.502. M.243.1932.II.A., section XII.)

² As calculated by the Research Department of the Federal Reserve Bank of New York. The calculation takes account of other elements of the price-structure than wholesale commodity prices, as, e.g., wages.

*The Movement of Prices in the United States of America,
1929-1932.¹*

(Average 1929 = 100.)



¹ Indices for the General Price Level and the Cost of Living and Wages (average weekly living rate for unskilled labor) published by the Federal Reserve Bank, New York —, Wholesale Price Index of the U.S. Bureau of Labour Statistics; Index of Security Prices calculated for fifty Stocks by the *New York Times*.

Even when attention is centred upon wholesale commodity prices alone, and upon the decline, unprecedented in its rapidity, depth and persistence, which has lasted from 1929 to the present time, it is evident that behind such a movement there must lie very difficult and obstinate maladjustments of the economic system. An attempt has already been made to analyse this background¹ and, in the first section of this chapter, attention was drawn to the symptoms of price instability which were apparent before 1929. The remainder of this section will deal with the actual course of wholesale prices in 1929-1932, and the following sections will be devoted to some of its complications.

The average level of wholesale prices had been falling in many countries long before the New York stock market collapsed in October 1929. The international adjustments referred to previously² obscured the situation but, from the beginning of 1929 at least, there was in most countries a tendency for prices to fall. This falling tendency gathered strength until, with the breakdown of the speculative boom, it became precipitous. The diagram which follows shows how universal was the fall in gold prices and how heavy it has been, especially in the agricultural debtor countries such as Australia, the Argentine, the Dutch East Indies and India.

The course of prices seems fairly clear, at any rate in the first two years of the depression. Prices fell fastest in 1930 in the agricultural countries, represented in the diagram by Australia, India and the Argentine. Japan was not far behind in the deflation and Italy also suffered heavily. As early as 1930, there were evident signs of strain in the agricultural debtor countries, and Australia and Argentine were already off the gold standard.

In 1931, the pace of deflation showed no signs of slackening and its incidence was particularly heavy on the remaining agricultural country in the list—the Dutch East Indies. Before the year was ended, however, the pace had proved too hot for many countries. Great Britain, India and Japan were off the gold standard, and the variations beginning to appear in the other index-numbers are evidence of artificial support to the price-level, even in countries nominally on the gold standard. By the beginning of 1932, the average fall in gold prices in those countries which had adhered to the gold standard was about 30 per cent from the levels ruling in December 1929 or 30-35 per cent from the average of that year.

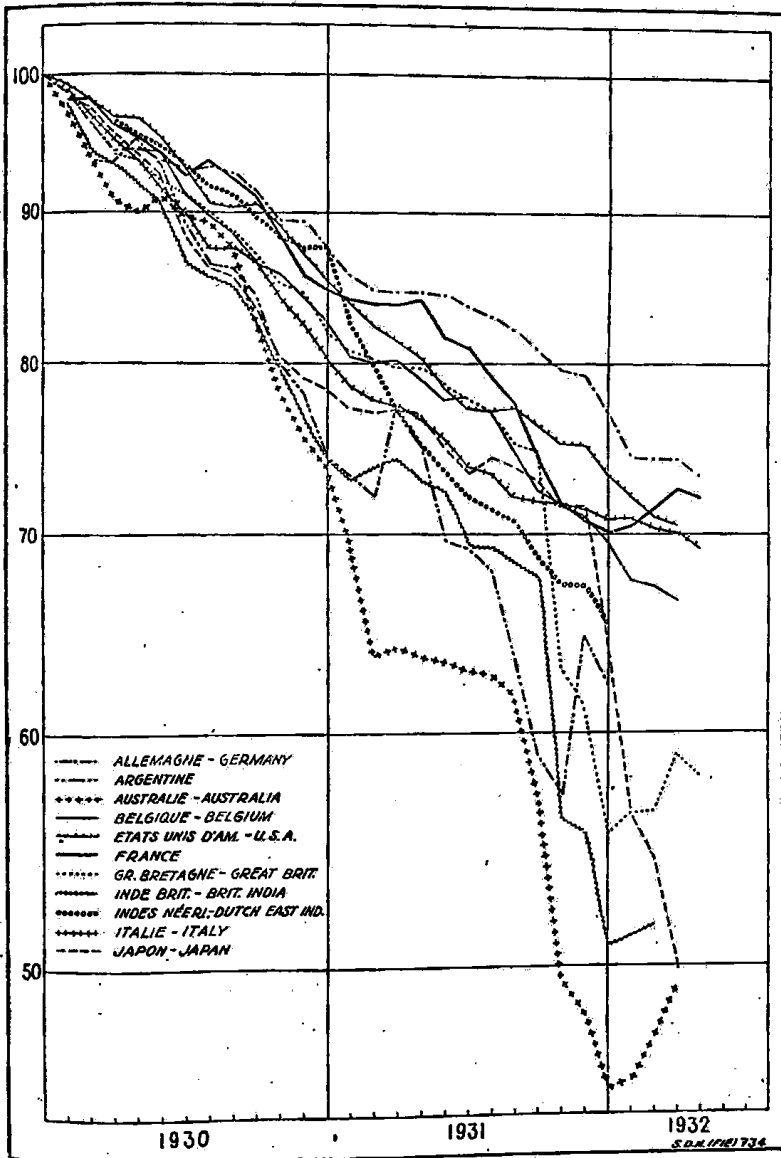
This estimate of a 30-35 per cent fall in gold prices between 1929 and 1932, however, is calculated from national price

¹ See Chapters I and II.

² See section (i).

Wholesale Price Movements in Terms of Gold, 1929-1932.

(December 1929 = 100.)



— the South-American States, Great Britain, the British Empire, and the British Dominions (with the exception of South Africa), and the Scandinavian States, as well as other countries such as Portugal, Egypt and Siam — are now operating paper currencies. For many of these countries, sterling tends to offer an alternative and moderately stable standard. The strength of sterling has been displayed, not only by the remarkable steadiness of domestic wholesale prices within Great Britain, but also by the fact that, instead of import prices being forced up to the full extent of the exchange depreciation, gold prices fell more heavily after Britain abandoned the gold standard. Between September 1931 and March 1932, gold prices, as measured by the London *Economist*, fell 10 per cent, while sterling wholesale (but not retail) prices of the same commodities rose 16 per cent — a result which corresponded roughly with the exchange depreciation at that time. It is of little value, however, to calculate purchasing-power parities on the crude basis of a combination of exchange rates and wholesale price index-numbers. The influence of financial factors, as well as commodity prices, is very great, and it is not possible to measure these factors with any exactitude. The important fact is that the trading world is now faced, not with one, but with several international standards of value, and that the relation between price-levels expressed in these various standards is constantly changing. The continued tendency of gold prices to fall, though still an important factor in prolonging the depression, is less important than it was. In those countries which, like Great Britain, have abandoned the gold standard without unsettling the domestic price-level, there is evident progress, not only in arresting the long-continued decline, but also in readjusting the disequilibria which were part of the cause of, but were also aggravated by, the decline of gold prices.

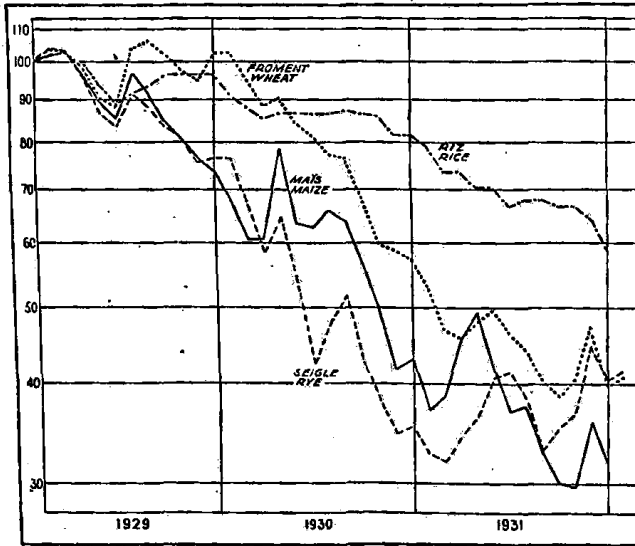
(iii) THE COMPLICATIONS OF FALLING PRICES.

(a) *The Course of Individual Commodity Prices, 1929-1932.*

The preceding section of this chapter has described the very heavy and almost universal fall in the average levels of wholesale commodity prices during 1929-1932. These levels, however, are constituted by averaging price-movements of large numbers of different commodities and, as the diagrams which follow clearly indicate, there have been remarkable differences of movement within the average. It is obvious that each commodity or group of commodities has special conditions affecting its price ; but, in

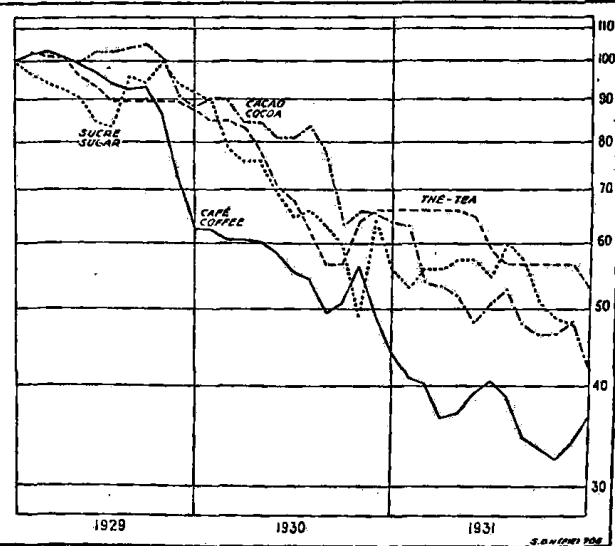
*Wholesale Prices in World Markets of Certain
Cereal Products, 1929-1932.*

(January 1929 = 100.)



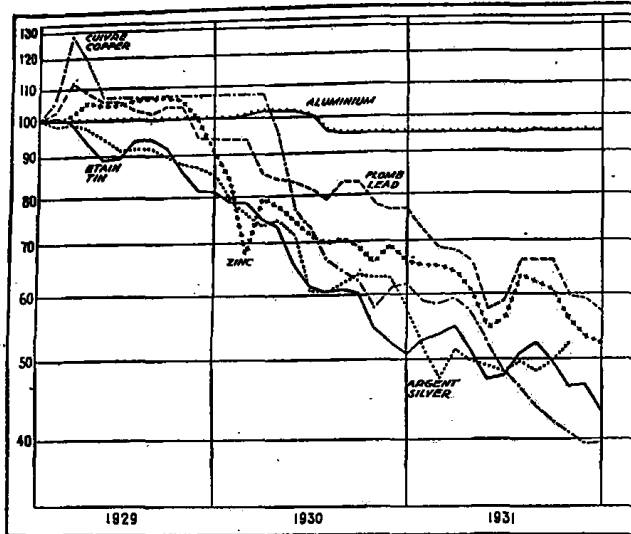
*Wholesale Prices in World Markets of Certain
Colonial Products, 1929-1932.*

(January 1929 = 100.)



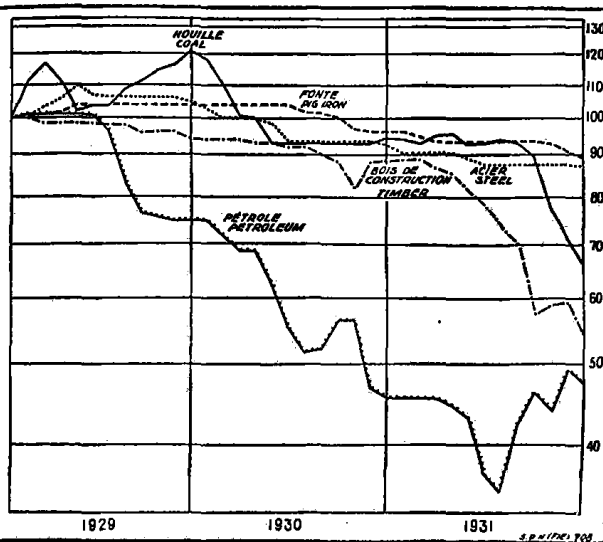
*Wholesale Prices in World Markets of Certain
Non-Ferrous Metals, 1929-1932.*

(January 1929 = 100.)

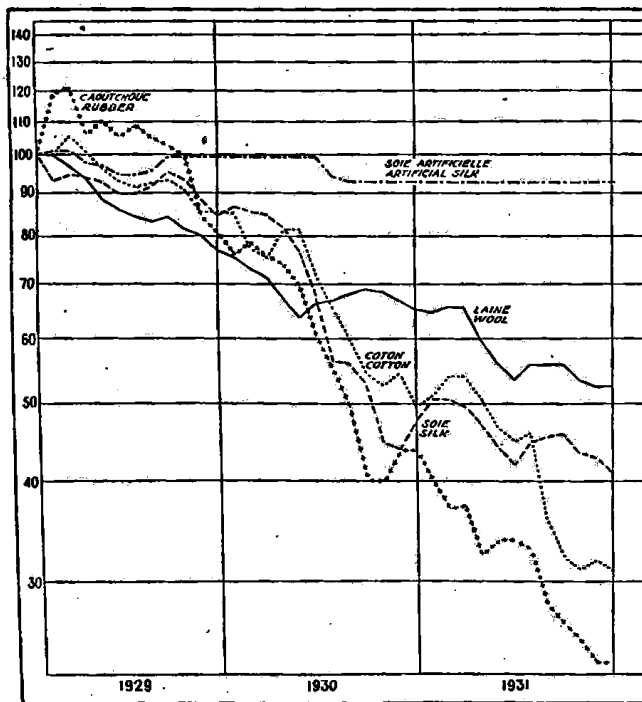


*Wholesale Prices in World Markets of Certain
Iron Products, Non-Metallic Minerals
and Timber, 1929-1932.*

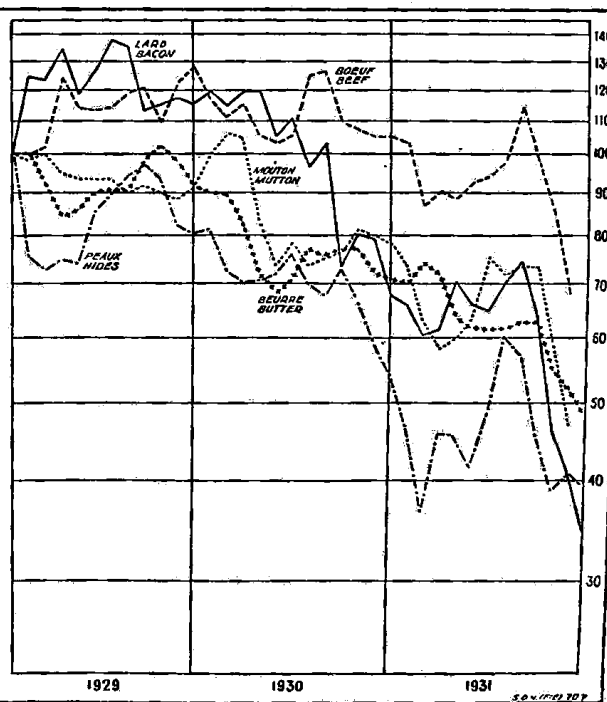
(January 1929 = 100.)



Wholesale Prices in World Markets of Certain
Textile Products and Raw Rubber, 1929-1932.
(January 1929 = 100.)



Wholesale Prices in World Markets of Certain
Animal Foodstuffs and Hides, 1929-1932.
(January 1929 = 100.)



addition to the fluctuations in demand and supply caused by factors peculiar to the particular commodity concerned, there were, in the depression period, two other important disturbing influences. The first was the interference with normal price adjustment caused by controls and valorisation schemes and, more successfully, by cartels and trade organisations. From the middle of 1929 to May 1931, for example, the Federal Farm Board in the United States bought wheat in large quantities. The Coffee Institute of Brazil temporarily checked the decline in coffee prices in late 1930. Efforts to limit production and sustain the price of sugar were continued throughout 1930. Similar attempts were made by concerted international action to check the fall in important mineral products such as copper, tin, lead, and zinc. Though in practically every case the success of such valorisation schemes was limited and temporary, they were important, not only because they maintained prices for a time, but also because the ultimate fall in prices was so greatly aggravated, both by the increased production, which was encouraged in many cases, and by the accumulation of stocks which had eventually to be thrown on to an already weak market. The rubber restriction scheme is a convincing example of the encouragement to production, and the experiences of the Brazilian Coffee Institute and the Federal Farm Board illustrate the depressing effect in the long run of endeavouring to keep prices up by withholding stocks. The more effective industrial cartels, on the other hand, as is shown later, have been more successful over a longer period, largely because they could control production as well as price.

Moreover, such attempts at price control rendered more difficult and irregular the second complicating influence on price movements — viz., the industrial maladjustments and disequilibria created by a drastic decline of the average level. The decline of prices, precipitated by structural maladjustment, became in turn a cause of further maladjustment. Occasionally, there was a curiously favourable effect on certain industries, as when the much more rapid fall in cereal than in animal products gave an advantage to the dairy farmers of Denmark and similar countries. In these highly organised farm industries, cows are equivalent to machine equipment and their food to raw material. The cheapening of raw materials relatively to the finished product placed butter, cheese, bacon and meat in a relatively favoured position during most of 1930.

For the most part, however, the reactions of falling prices of commodities, one upon the other, have been less fortunate. Commodity prices have tumbled one after the other, each bringing down joint-products, by-products and substitutes in its

fall. Moreover, purchasing power has been more and more constricted, since certain charges upon industry — wages, interest, taxation — have remained fixed in terms of an appreciating currency, and every fall in the price of a commodity tended to restrict the purchasing power of its producer still further.

It is significant that the commodities which began to fall first were certain cereals and textile raw materials — rye, maize, wool, flax were all falling heavily from the early part of 1929, long before the boom came to an end. Petroleum, silver and tea were also falling at this time. After the collapse of the boom some of the heaviest falls took place in coffee, flax, maize, rubber, wool, petroleum, tin and silver. In many of these cases, control schemes had broken down. In almost all cases, the fall in prices was a serious matter for the raw-material producing debtor countries. The behaviour of individual commodity prices in the months immediately before and after the crisis of October 1929 supports the argument previously advanced¹ that the plight of the debtor countries, after the shrinkage of capital imports in late 1928, was a main cause of the depression.

When raw-material commodity prices began to fall so heavily in late 1929, the general average of wholesale prices naturally moved downward. But there was strong resistance to price reductions, particularly in the case of those commodities the production of which could be relatively easily controlled. The prices of manufactured goods have, on the whole, fallen less than those of raw materials, because it is generally easier to curtail production by closing a factory than by abandoning a farm or shutting down a mine. Succeeding sections of this chapter will be devoted to some important aspects of the variations in price movements arising from these causes.

(b) *The Influence of Cartels and Trade Organisations.*

The influence of cartels and trade organisations has been more successful than the somewhat similar agricultural valorisation schemes in checking the fall in prices of certain important groups of commodities. The policy of these organisations is generally to maintain stable prices in good times and bad; the fluctuations in demand which take place in the various phases of the business cycle are accordingly countered by fluctuations in output rather than in price. Where the producers' association is national in scope it is in most cases aided in maintaining domestic prices by means of tariff barriers. In some instances, indeed, a differential price policy is pursued, and sales in foreign

¹ See Chapter II.

markets are made at a lower price than sales in the home market. Where the agreement is international, it often includes an understanding on the part of the various producers not to sell in each other's markets. Unfortunately, serviceable indices for "cartellised" and "non-cartellised" prices are available only for Germany, where it is estimated that half the industrial raw materials and semi-manufactured goods (as measured by the numbers of workers employed in producing them) fall within the former category. The success of the cartels in maintaining prices in this country may be judged from the following table:

Price Indices of Cartellised and Non-Cartellised Industrial Raw Materials and Semi-Manufactured Goods in Germany, January 1929-1932.

(1926 = 100.)

	Cartellised	Non-Cartellised
January 1929	104.6	101.9
January 1930	105.0	90.4
January 1931	95.2	66.2
January 1932	84.4	51.2
Percentage decline, January 1929 to January 1932	19	50

Source: *Vierteljahrshefte des Instituts für Konjunktürforschung.*

The index for cartellised prices is not completely accurate, since it is based on price lists and does not take into account reductions granted in the form of cash discounts, rebates, etc. The magnitude of the discrepancy is, however, significant. Cartellised goods in Germany would appear to have fallen only one-half to one-third as much as "free goods". The full significance of this fact is grasped only when it is realised that the cartellised goods in Germany (and elsewhere) are for the most part "producers' goods", such as iron and steel, which are destined for capital equipment—*i.e.*, real investment—whilst the "free" goods are largely used in making articles destined for final consumption. The discrepancies in the movements of these groups are further discussed below.

Cartellised prices in Germany dropped somewhat more rapidly in 1931 than in 1930¹ as the result of governmental

¹ It may be noted that, while free prices rose 12 per cent in the boom of 1927, cartellised prices did not follow them. This helps to explain the investment boom of that year in Germany.

pressure as well as of economic conditions. Practically the whole of the decline from January 1931 to January 1932 took place after the emergency Decree of December 1931, which required all cartels to reduce their prices by 10 per cent below those of June 30th, 1931. The index for cartellised prices (1926=100) stood at 93.4 in November 1931 but fell to 84.4 in January 1932 and slightly lower in February. In the latter month, it was slightly more than 10 per cent below the level of June 1931. It should be noted, however, that, with the exception of Italy, no other great industrial country has yet applied governmental pressure to reduce costs of production and manufactured prices in the way described above.

(c) *The Severity of the Fall in Raw-Material Prices.*

During the years 1929-1932, as indeed in all depressions, raw materials have fallen in price more sharply than finished goods in every country. The following table will show how marked is the difference in the rate of decline.

Percentage Fall in Wholesale Price Indices of Raw Materials and Manufactured Goods in Certain Countries, January 1929 to January 1932.

	Raw materials (Percentage)	Manufactured goods (Percentage)
Canada	38	22
Germany	31	21
Italy	44	30
United States of America	39	26

The greater part of the discrepancy between the prices of raw materials and manufactured goods developed in the earlier stages of the depression. In the year 1930, raw-material prices fell very heavily, but there was a considerable lag in the prices of finished products. In 1931, the rapidity with which raw-material prices declined slackened somewhat, while manufactured goods began to fall faster in most countries than they had fallen in 1930.¹ Even then, however, raw-material prices were falling at a more rapid rate, so that the discrepancy was still being widened, though at decreasing pace. This development is clearly shown by the following table :

¹ In Italy, the slower decline of the prices of finished products in 1931 is partly explained by the heavy fall in 1930 and the even heavier fall in 1929.

*Percentage Fall in Wholesale Price Indices of Raw Materials
and Manufactured Goods in Certain Countries
in 1929 and 1931.*

(Fall from January to January in each case.)

	Raw materials			Manufactured goods		
	1929-30	1930-31	1931-32	1929-30	1930-31	1931-32
Canada	+4	32	12	—	14	10
Germany	4	16	14	2	9	12
Italy	10	24	17	12	12	9
United States ¹	5	21	17	3	12	12

The reasons for this discrepancy (which occurs in every period of depression) between the price-movements of raw materials and finished goods, are fairly clear. There is naturally a lag in the prices of finished products, since the processes of production occupy a fairly long period. Moreover, this lag is increased by the fact that merchants and manufacturers carry reserve stocks of raw materials. It takes some time for a change in the price of raw materials to be reflected in the prices of finished goods.

In addition, the producers of raw materials are, on the whole, in a weaker bargaining position. This is especially true of the scattered agricultural producers. Where the raw materials of industry must be produced by large-scale industrial methods, as in the case of many minerals, production and price-control is more readily possible. This, it is argued later, is the primary reason why the prices of producers' goods (capital equipment) have been relatively better sustained than those of consumers' goods. The heavy fall in raw-material prices, however, is mainly a reflection of the weak bargaining power in the world's markets of unorganised agriculturalists. Valorisation schemes, controls and pools have been much less successful than cartels and trade organisations; production has been difficult to restrict; stocks cannot be kept for long off the market. Moreover, it is not possible by lowering prices of raw materials to stimulate demand as quickly, directly and effectively as in the case of finished products. A substantial decline in the price of raw materials may not cause more than a slight decline in the finished product, so that, even if consumer's demand is somewhat stimulated, that stimulation is not in proportion to the lower receipts

¹ December 1931 instead of January, 1932.

of the raw-material producer. Costs of production tend to be more rigid in the finishing processes which require more capital equipment and highly organised labour. It is inevitable, therefore, that raw-material prices are driven downwards at the expense mainly of the agriculturists.

In the present depression, the decline in agricultural prices has been extremely severe, particularly in the countries outside Europe which produce cereals and textile raw materials. In Canada, the United States, Australia, New Zealand, and the Argentine, the fall in agricultural prices averaged round about 50 per cent from the beginning of 1929 to the beginning of 1932.

The decline in purchasing power caused by such a heavy fall of prices, even if it is somewhat offset by increased production, is a serious factor in the prolongation of the crisis. In the United States, it is estimated by the Department of Agriculture at about 50 per cent, in Germany at about 30 per cent¹ between 1929 and 1931. Nor is this decline in purchasing power fully compensated by a corresponding decline in the commodities and services the farmer must buy.² In New Zealand, the specially constructed official index of farm expenditure was almost stationary in 1929 and 1930, but the prices of farm products fell by 22 per cent. The price index of articles bought by farmers in the United States of America fell by 21 per cent from the beginning of 1929 to the beginning of 1932, whereas the farmers' purchasing power declined by 50 per cent.

These comparisons may tend to exaggerate the extent to which agricultural communities are adversely affected by the unequal incidence of falling prices, since the farm provides a substantial part of the living of the farmer and a comparatively small part of his real income is spent on industrial products. But the marked discrepancy which exists between the prices of agricultural raw materials and those of finished products, and the reduced purchasing power of the agriculturalists obviously set a limit to industrial recovery. Until the prices of raw materials and finished products can be brought into equilibrium again, there will remain a vicious circle of falling prices, decreased purchasing power and reduced employment. The widening of such a "scissors" in the price-structure is always a symptom of industrial maladjustment, and its closing is an essential condition of recovery.

¹ *Wochenbericht des Instituts für Konjunkturforschung*, December 9th, 1931.

² There was, during 1929 and 1930, a sharper fall in cereals than in animal products, so that meat and dairy farmers gained a substantial relative advantage. But the shift from arable to animal farming caused a sharp fall in the prices of animal products in 1931.

(d) *Producers' and Consumers' Goods.*

The preceding sections of this chapter have been devoted to an analysis of some of the complications in the price-structure created by the uneven movements of the prices of different commodities and commodity groups. The drastic fall in the average level of wholesale prices, important and difficult in itself, is rendered more difficult because the rapidity of the fall throws the relations of price-groups into confusion. Almost any grouping of price-movements could be used to illustrate the extent to which the complex and interdependent price-structure has been thrown out of gear, but particular importance attaches to the distinction between the prices of commodities destined for final consumption and those used for capital equipment. Indices are available in some countries which measure the price-movements of consumers' goods as contrasted with producers' goods, and the evidence of maladjustment which they provide throws light on a central cause of the persistence of depressed conditions.

In previous depressions, producers' goods destined for capital equipment fell more heavily in price than consumers' goods. In the nineteenth century, mineral prices especially fell rapidly and severely in every depression. For later crises, definite index-numbers are available. They show that, in the crisis of 1907-8, producers' goods in the United States fell by 15 per cent, while consumers' goods fell by 7 per cent. In Germany, in the same crisis, producers' goods fell by 24 per cent and consumers' goods by 9 per cent. During the depression of 1920-1922, the relevant price indices show similar movements in Canada and the United States.

During the present depression, however, precisely the opposite movement has taken place; capital equipment and the materials for capital equipment have fallen much less in price than have consumers' goods at corresponding stages of manufacture. In Canada, for example, the price of producers' equipment reached its highest point in April 1930 and from then until the beginning of 1932 fell only 5 per cent. Consumers' goods, on the other hand, in the same period, had fallen by almost 25 per cent since 1929. In Germany, at the beginning of 1932, finished consumers' goods had fallen by 27 per cent since the beginning of 1929 and finished producers' goods by only 11 per cent. In the United States of America, the National Bureau of Economic Research index for articles of capital equipment fell by 21 per cent between January 1929 and October 1931, while the index for articles of human consumption fell by 35 per cent. For Italy, specially

prepared indices of producers' and consumers' goods show that producers' goods were 19 per cent lower in 1931 than in 1929, while consumers' goods were 29 per cent lower.

These facts point to one of the main obstacles that stands in the way of recovery from the present depression. Previous depressions were gradually overcome when capital goods became cheap enough, in relation to the prices of consumers' goods, to tempt business enterprise once more to expand its operations. The preceding boom period in such cases was most marked in the industries devoted to producers' goods. When depression developed, therefore, there was an expanded production of these capital goods and a strong tendency for prices to fall. Moreover, general purchasing power was never before so badly affected as it has been in the present depression, and consumers' demand kept up relatively well, so that the prices of consumers' goods were less affected.

The present depression, on the other hand, was preceded by a marked boom in consumption and particularly by an inflated demand for articles of durable consumption, accompanied by widespread growth of debt encouraged by instalment selling. The collapse of purchasing power in the depression, aggravated by the unusual debt commitments, has been unprecedented, so that the prices of consumers' goods have fallen heavily. On the other hand, there has been strong resistance from the powerfully organised capital-equipment industries, many of which are cartellised and, in the process of organisation, have been loaded with excessive capital obligations. Capital costs, labour costs, and prices have remained much more rigid in these industries. Demand has fallen off and production decreased to what in former depressions would have been regarded as catastrophic levels; but prices have been slow to fall. The steel industry, particularly in the United States, is a good example of this development.

Until this deadlock is broken in some way, either by the prices of consumers' goods rising, or by a reduction in the prices of producers' goods, there is little possibility that industrial profits will re-emerge, tempting business to expand. There is a fundamental maladjustment at this point which blocks the efforts of governmental or monetary or business leaders to start the processes of recovery.

(e) *The Segregation of Domestic Markets.*

In describing the collapse of prices in the years 1929-1932, stress was laid upon the severity of the fall in the wholesale

prices of commodities.¹ and it was pointed out that the fall had been greatest in those commodities which are described as sensitive — mainly commodities which enter freely into international trade. One of the most marked features of the depression has been the concentration of selling pressure upon the export surpluses of these products. In the later stages of the depression, however, there has been a definite movement towards segregating and protecting the domestic markets, and it becomes more and more difficult therefore to measure the true extent of the decline which is actually taking place.

This movement, already strong, was immensely reinforced after the gold standard was abandoned by many countries in the latter part of 1931. Up till then, the monetary systems based on gold provided a common denominator in which individual prices and national price-levels might be compared. Tariffs, contingent systems, quotas, milling and similar regulations were being multiplied, so that domestic prices diverged more and more from prices of the same commodities in international markets. But the international markets remained powerful and set the basic prices of which domestic prices were varying functions. Moreover, the necessity of keeping the exchanges stable set a limit to the extent to which the average of domestic prices might rise. If the prices of some commodities were heavily protected, a general rise in prices could be avoided only by depressing the prices of other goods. The abandonment of the gold standard took away this restriction and it is now more possible for domestic price-systems to fluctuate independently instead of being restrained by international influences. There are limits to this possibility; but the partial destruction of the organised world markets for staple commodities must be reckoned as one of the casualties of the falling price-level.

The extent to which countries still on the gold standard have managed to segregate their domestic markets may be illustrated by the following table, in which the price indices of various groups of raw materials in Germany are shown for the beginning of each year since 1929.²

¹ See section (ii).

² These indices were prepared by the Statistisches Reichsamt for the use of the League of Nations in a special enquiry into relative price movements and will subsequently be treated in greater detail along with those prepared by certain other countries.

*Price Indices of Various Groups of Raw Materials in Germany,
January 1929 to January 1932.*
(1913 = 100.)

	(1) Vegetable foodstuffs	(2) Animal foodstuffs	(3) Vegetable raw materials	(4) Animal raw materials	(5) Mineral raw materials
January 1929.	133.4	126.9	127.4	136.1	119.3
January 1930.	113.9	128.1	117.6	99.6	120.3
January 1931.	110.4	106.4	73.5	74.5	105.2
January 1932.	113.1	77.5	54.3	51.0	93.0
Percentage de- cline, Janu- ary 1929 to January 1932	15	39	57	62	22

Animal foodstuffs and vegetable and animal raw materials appear to have followed world-market prices quite closely, but the 15 per cent fall in raw-vegetable foodstuffs in Germany may be compared with a decline in this group on world markets ranging from 40 to 70 per cent, and the 22 per cent decline in mineral raw materials may be compared with a fall for similar commodities on world markets ranging, in most cases, from 30 to 50 per cent.

The discrepancy between the movement of internal and external prices is by no means confined to Germany, but is shared by many other countries. The following table shows the percentage decline in the prices of domestic and imported commodities in four European countries between January 1929 and January 1932.

*Percentage Decline in Prices of Domestic and Imported Goods,
January 1929 to January 1932.*

	Domestic goods	Imported goods
Germany	21	49
France	25	54
Czechoslovakia	22	35
Sweden ¹	22	37

¹ January 1929 to September 1931.

The groups "domestic" and "imported" goods do not, of course, contain identical articles, and the figures shown above are therefore in no sense an exact measure of the difference in the fall in prices of the *same* goods on world and home markets. None the less, the discrepancies are very striking. They are to be attributed in the main to two factors : first, to the special measures which have been taken by Governments to protect the prices of some domestic products against the fall in world-prices ; second, to the fact that cartels and other price-fixing producers' associations have, in many cases, been successful in maintaining their domestic prices, in addition, as has been pointed out above, to maintaining world-prices for their goods at a relatively high level.

The methods by which this segregation and protection of the domestic markets have been brought about are all those devices of economic nationalism which have been multiplied since the war and especially in the latter stages of the depression. Tariffs have been raised, import contingents imposed or quotas supplemented by clearing agreements, exchange regulations have controlled the available amounts of foreign exchange, specific duties have become more effective as prices fell, administrative regulations (and fees), and indeed the whole apparatus of state regulation, have in many countries been directed towards cutting off the domestic from the world market and protecting the former against the severity of the price decline on the latter.

Such measures have the double effect of concentrating and intensifying the price decline on world markets and of destroying the regulatory value of competitive trading. Domestic prices are maintained so that production (already excessive) is further stimulated at the places where its costs are high.

The prices of wheat, one of the most universal world products, in domestic markets, as shown in the following table, offer striking evidence of the extent to which the world markets have been shattered.

*Domestic Prices of Wheat in Various Countries,
January 1929 and January 1932.*

	In United States cents per bushel of 60 lb.	
	January 1929	January 1932
Argentina	113	44
Canada	120	51
Great Britain	123	53
United States	121	58
India	158	60
Hungary	158	60
Poland	140	81
Sweden	137	91
Austria	131	120
Czechoslovakia	147	121
Germany	135	147
Italy	192	151
France	164	179

It is obvious that this retreat from international economic co-operation is another strong factor in prolonging the depression, since it concentrates and intensifies the falling-price tendencies on export markets and thus retards the recovery of the raw-material producing debtor countries the weakness of which precipitated and has prolonged the depression. The recovery of production and trade, essential to any improvement in the industrial countries, is just as dependent upon the restoration of purchasing power in the agricultural countries as that restoration is dependent upon the industrial countries opening their markets once again.

During 1931, there was some evidence that domestic prices in several industrial States were beginning to be adjusted more rapidly to world prices. Thus in France, the domestic level of wholesale prices fell by 6 per cent in 1930 but by 16 per cent in 1931. But this was a passing phenomenon, and the renewal of financial strain in the latter half of 1931 caused a reversion to policies of economic isolation. Only in countries where vigorous extraordinary measures of domestic readjustment have been taken, as in Germany, Italy, Australia and New Zealand, have domestic price-levels fallen rapidly. The abandonment of the gold standard

by many countries (including Australia and New Zealand) has achieved much the same result, but has been accompanied by an intensification of the falling tendency of prices in countries remaining on the gold standard. The situation in the spring of 1932, therefore, is that international equilibrium of the price-levels has been destroyed and international trade is in some danger of perishing in the confusion.

(iv) THE RESTORATION OF EQUILIBRIUM.

The foregoing analysis of price movements in the depression years indicates how widespread and confusing have been the effects of the fall in the general level. The economic organisation of the world has been thrown out of gear. Internationally, the price-levels of various countries have parted company, since so many countries have abandoned the gold standard. There has been created, moreover, a wide disparity between domestic levels of prices and the prices of those export surpluses which must seek foreign markets. Those agricultural countries which have been placed under double pressure by the enhanced burden of their debts and the very heavy fall in the prices of raw materials and foodstuffs have become a source of weakness in the whole world system. The flow of capital has ceased, existing financial commitments are jeopardised, and the currency systems in many cases are gravely compromised. In all these ways, a serious blow has been struck at international economic co-operation.

Within the economic, as distinct from the political, structure of the world, equally serious situations have arisen. After a period of credit expansion in which agricultural prices were artificially sustained and production over-extended, there has been a very drastic fall in prices, partly counteracted by the protection of domestic markets. The restriction of production, which normally corrects such a situation, takes time to develop, and is, moreover, a very serious step to take in the case of many of the countries concerned.

Retail prices, the cost of essential services both public and private, the cost of living, wages and costs of production generally, lag behind changes in the wholesale prices of commodities. This lag is always evident and causes distress and suffering in all depression periods, because of the uneven incidence of the price decline on various classes in the community. Not all occupations suffer heavily ;

some, indeed, gain when average prices fall without a corresponding diminution of the rewards for their services. But when the price decline is as rapid and severe as it has been since 1929, the general weakness of economic life which results from abnormal price relations affects almost every section of the community adversely. Certain prices may be sustained, but turnover diminishes; wages and salaries are reduced with difficulty, but unemployment increases; the *rentier's* share of the national income apparently rises in real value; but security values decline, moratoria are declared and taxation is raised.

The worst difficulties arise, however, from the dislocation of economic activity caused by the abnormal price relations that develop. Attention has been drawn to some of the more important aspects of these difficulties and, in particular, to the unusual relation in this depression between the prices of consumers' goods and producers' goods. As in every great crisis, economic or political, the essential problem arises of discovering the means by which economic activity shall once again be restored. There are difficult problems of maladjustment and injustice; but the really serious matter is the paralysis of production and interchange. If this paralysis can be overcome and economic activity resumed, the maladjustments and injustices can be remedied.

The way out of former depressions has normally been by such reductions of the costs of production as offer prospects once again of business profits. Wages are lowered, interest rates decline, and, perhaps most significant of all, the prices of typical investment goods or producers' goods fall relatively more than those of consumers' goods. It is by the widening of the margin of profit between the costs and the turnover of industry that enterprise is revived, investment stimulated and economic progress resumed.

At this point in the present depression, however, there has been a deadlock. Raw-material prices as a whole have fallen heavily, but prices of finished goods have not fallen as much. Wages are difficult to reduce, and interest rates, partly because of the higher risk premia demanded in a period of failing confidence and stringent credit, partly for reasons connected with the changed nature of capital savings,¹ remain high.

Moreover, within the category both of finished manufactured goods and of raw materials there is a further block, since producers' goods and the materials for their manufacture have fallen less in price than consumers' goods and their raw materials.

¹ See Chapter I, section (vii).

The control of production is easier in the case of minerals, which form the most important group of producers' raw materials, particularly since the most important industrial minerals are now produced by large-scale methods involving heavy capital expenditure.

The difficult situation has been created, therefore, that prices of finished goods are too high relatively to raw materials, and producers' goods relatively to consumers' goods. In previous depressions, recovery has taken place when the cheapening of raw materials together with reductions in the costs of manufacturing production and lower prices for capital equipment have lowered the prices of finished products to levels within the buying capacity of the consumers. In the present depression, the buying capacity, particularly of agriculturists, has been depressed so much that, even were manufacturing costs less rigid, there would be great difficulty in bringing them down to an equilibrium with the purchasing power of consumers. In fact, however, there has been great resistance to writing-down the claims of capital, labour or the tax-gatherer. In addition, the producers who have to supply the demands of the consuming public find their capital equipment still relatively expensive. The world needs a larger production — for example, of steel and steel products — at lower prices, and a smaller production of most foodstuffs and textile raw materials at higher prices. But neither adjustment is easy to make. The industrialist finds it easier to reduce production than to lower costs, and the farmer cannot afford to restrict his output while his prices are falling.

Practically all students of the depression agree that this deadlock is the crucial problem to be faced, but opinions differ widely as to the best method of overcoming it. Two alternative lines of policy are widely discussed, each with many variations, but both starting from the view that the basic cause of the present deadlock is to be found in the discrepancies between costs and selling prices.

The first alternative is to seek an adjustment to the low level of prices now prevailing for raw materials. It is argued that the rigidity of costs in the highly organised manufacturing industries, and particularly in the capital-equipment industries, sustains the prices of finished goods at a level beyond the purchasing capacity of large groups of the community. Consequently, manufacturers cannot sell the former quantity of their products to the producers of raw materials and will not be able to do so until their costs and prices are scaled down to their pre-crisis relationship with the prices of raw materials. If this scaling down takes place, then — even though wages in manufacturing

industry will be lowered — the wage-earning class as a whole will benefit by a lower cost of living and by the increased employment which results from the greater ability of primary producers to buy manufactured goods. The expansion in industrial output will, in turn, create a demand for raw materials which will stop the fall in their prices and, in this way, a new equilibrium will be reached.

The economic efforts of the world have, according to this theory, been largely concentrated, during the past two or three years, on resisting liquidation. This is true, not only of labour costs in industrialised countries, but also of capital charges, and is especially evident in the industries producing capital equipment or producers' goods. Firms which, before the depression, borrowed (or watered) capital on what is now regarded as an inflated basis have not been forced into insolvency but have often, either through their own internal strength or through outside financial assistance, been successful in keeping their inflated capital structure intact. The interest which must be paid acts as a deadweight on industry, and leaves, under the lower level of prices now prevailing, little if any margin for profits. Unsound and relatively inefficient concerns have not been forced into bankruptcy to the same extent as during previous depressions, so that the main salutary effect of such a period of liquidation has not been achieved. In order, therefore, to reach a sound foundation from which recovery may take place and to stimulate recovery, the proponents of cost reduction urge that both labour and capital costs in manufacturing industry should be reduced so that the prices of manufactured goods may be more comparable again with the prices of raw materials.

The advocates of measures to raise the price-level also start from the view that the discrepancy between costs and selling prices is an essential factor of the depression, but they deny that the relationship between the two, and particularly between wage reductions and lower prices, is as close as is often assumed. Moreover, it is argued, even if the selling price of the finished product is lowered, this will not necessarily be in the same proportion as the particular element of cost is reduced. It is not clear, therefore, that the immediate loss in purchasing power in the industrial community will be made up by a proportionate expansion in the demand of the raw-material producing community, for the demand of the latter depends upon its ability to finance purchases of, as well as its desire for, manufactured goods. It is urged further that, if an equilibrium between the prices of raw materials and of manufactured goods is sought by a scaling down of production costs, the reduction would need to be so great as to be practically inconceivable. If raw-material

prices remain at their present level and industrial goods must be reduced 25 per cent to bring them into equilibrium, the magnitude of the cost reductions involved is very great. An elastic capital structure, such as the proponents of cost reduction wish for and often assume, would no doubt be desirable, but, unfortunately, it does not exist, and so the brunt of the burden of reduction would have to be borne by labour cost. Moreover, though it is true that unsound enterprises have, in many cases, not gone into liquidation, it is argued that the soundness or unsoundness of an enterprise is itself largely a function of the level of prices prevailing at any given time, and, if prices fall sufficiently low, no enterprise whatever is sound.

Accordingly, the proponents of the second alternative urge that the price deadlock should be broken by a levelling upwards rather than a levelling downwards. They differ as to the methods which could and should be used, but unite in urging that, though some cost adjustment in manufacturing industry may be necessary, an effort should be made also to raise the level of raw-material prices. In this way, they urge, most of the discrepancies discussed above will be narrowed; the necessity for painful adjustments of income will be reduced; and the burden of debt, public and private, which has been so greatly increased by the fall in prices, will again be lessened. The rise in the prices of primary products will increase the buying power of the classes affected, enable manufacturing industry to work at greater capacity and thus reduce its unit costs, and permit the general emergence of profits.

In view of the conflict which exists between these alternative theories — a conflict reflected in practical policies — it is as yet difficult to trace in the actual progress of events the particular combination of measures being pursued. Policy is rendered difficult and its results obscure, because of the existence of moratoria, standstill agreements, or other means of suspending the debt payments which form a large part of productive costs, directly or indirectly. In Germany, Italy, Australia, New Zealand and other countries, a direct attempt is being made to reduce the price disparities by governmental pressure on those prices which have hitherto remained relatively high. In the countries which followed Great Britain's action in abandoning the gold standard, some part at least of the necessary adjustment was found in the opposite direction by a scaling down of fixed charges through currency depreciation. Negotiations are in progress in many countries concerning more direct readjustments of both public and private debt charges. In the United States, definite governmental measures have been undertaken to stem the progress of currency deflation caused

largely by hoarding. On the other hand, the concentration of deflationary pressure on the prices of raw-material and foodstuff export surpluses appears to be having some effect in restricting the production of those commodities in many countries. There is thus little sign at present of any possible agreement upon a single heroic effort either to raise the average price-level or to scale down costs, and it is therefore impossible to foresee either the duration of the period of readjustment or the particular combination of methods by which readjustment will finally be attained. But the probability becomes clearer that there will be no single panacea. Individual countries will seek a new equilibrium by different methods, and the restoration of international equilibrium will follow gradually. There is no easy way of escape from such a confused and complex situation as that which has been outlined above.

Chapter V.

THE COURSE OF INTERNATIONAL TRADE.

(i) THE CHANGING NATURE OF INTERNATIONAL TRADE.

The rapid development of oversea trade, the opening up of new regions of settlement, and the industrial and urban concentration of Western Europe in the second half of the nineteenth century form a distinct and unique epoch in the history of foreign commerce. The application of steam-power to sea-transport, together with the railway-building which opened up the great continental areas of Europe and the Americas, Australia and South Africa, created a new kind of trade. Instead of rare and costly objects, large quantities of cheap, bulky goods of general demand — coal, mineral ores, grain, wool — became the characteristic cargoes. Industrial Europe sent out coal, railway equipment, machinery and manufactured goods and drew back raw-material resources from the rest of the world, nitrates from Chile, wool from Australia, grain from the prairies, and, after the advent of refrigeration, meat, butter and cheese from South America, Australia and New Zealand.

This comparatively simple trade, based upon cheap transport and facilitated by an increasing investment of capital in the developing agricultural countries, was dominated by British manufacturing, shipping, commercial and financial enterprise. But, in the latter part of the nineteenth and in the early twentieth century, even before the war, there were indications that international trade of this simple character, and the economic organisation and policies connected with it, were being challenged. The dominance of British banking, shipping, and commerce became less marked as other European nations sought industrial and trading outlets, the new agricultural countries began rapidly to develop their own manufacturing industries, and other centres of industry and trade grew up in North America and Japan.

One effect of the war of 1914 to 1918 was a marked strengthening of these tendencies to decentralisation of industry and trade. American and Japanese shipping and financial and commercial, as well as manufacturing, organisation developed

rapidly, and there was a marked increase also in the manufacturing output of such countries as India and China, as well as in that of Australia, South Africa and South America. The currents of trade became more complicated. New trade-routes were established, especially across the Pacific; shipping facilities were multiplied from North to South America, along the coast of Asia from India to Japan, and across the Pacific from North America to the Far East; the ports of the Far East, Singapore, Hong-Kong, Shanghai, Kobe, rose quickly to rank among the leading ports of the world; the Panama Canal within ten years of its completion carried as much traffic as the Suez Canal, and all the ports of the Pacific region — San Francisco, Vancouver, Honolulu, Suva, Auckland, Sydney, Manila, Sourabaya, Batavia — have grown rapidly with increasing trade. As in other parts of the world, the substitution of liner traffic for tramp-steamer services has made for the rapid growth of the larger, to some extent at the expense of the secondary, ports.

It is evident from such obvious and well-known facts that the nature of world trade since the war has undergone and is still undergoing very considerable changes. It is no longer dominated by the exchanges between industrial Western Europe and the raw-material producing countries, and its organisation is less centralised in the United Kingdom.

Successive issues of the League's *Review of World Trade* have drawn attention to the importance of the geographical changes in world trade that were so definite in the years immediately after the war. Up till about 1925, when the economic reconstruction of Europe began in earnest, the more rapid growth of trade in other areas, and especially the Pacific, was most marked. It was summarised in the *Memorandum on International Trade and Balances of Payments, 1911 to 1925*, as follows:¹

“ In comparing 1925 with 1913 figures, the United States and India now buy less from Europe and more from Asia; China and Japan buy less from Europe and more from North America; Australia less from Europe and more from both North America and Japan. Reciprocally, India sends a greater proportion of her goods to North America and Asia, China to North America; Japanese exports to Europe have dropped from 23 per cent to only 7 per cent of her total exports, while those destined for North America have risen from 30 to 45 per cent. Australian imports from Europe have dropped from 71 to 54 per cent of her total imports. . . .

“ Trade is passing from the Atlantic to the Pacific. ”

¹ Vol. I, page 164.

After 1925, however, there was a clear tendency for Europe to recover its lost ground. The movement of capital back to Europe and the great increase in productivity in the boom years 1925 to 1929 stimulated both the trade of European countries among themselves and their trade with the rest of the world. Many factors have contributed to this reversal of what had appeared to be an established tendency in the war and post-war trade. Among them, the effects of the reconstruction boom based upon cheap credit in the years 1925 to 1929 stand out as important. Connected also with the movement of capital back to Europe in this period, there went a movement of relative prices in favour of the manufacturing as distinct from the raw-material producing countries. Tariff increases and other measures of economic nationalism have reinforced these restrictive factors, and, in the years since 1926, these have affected agricultural products with especial severity.¹ As will be shown later, the disastrous fall of raw-material prices in the depression period and the concentration of its first effects upon the export surpluses of the raw-material producing countries still further restricted trade with the areas outside Europe.

In addition to these special and more temporary factors, however, there is apparently a change in the nature of international trade as a whole. Despite the fact that in the post-war years there were very large agricultural and mineral export surpluses thrown upon the world markets, there was before the depression a strong tendency for the proportion of raw materials in world trade to decrease. The import statistics of several important manufacturing countries showed a definite movement towards a higher relative proportion in the *quantum* of finished manufactures and a lower proportion in that of raw materials.²

A calculation of the changes in the *quantum* of world trade in primary goods as distinct from manufactured goods shows that in the period 1925 to 1929, this tendency was very marked.³ In those years, the trade in primary goods increased by nearly 15 per cent, but the trade in manufactured goods increased by roughly 31 to 32 per cent. These figures are not surprising, since the range of demand to which industrial progress caters is much more elastic than the first primitive wants for food, clothing and shelter. There is therefore a tendency for trade to develop most rapidly in manufactured goods and for this

¹ See Chapter X, section (ii). See also *The Course and Phases of the World Economic Depression*, pages 324 and 325.

² See Appendix I.

³ *Review of World Production, 1931.*

tendency to be most marked in periods of prosperity and expanding trade — a perfectly natural development in accord with the general progress towards a rising standard of living and a greater development of secondary production. The League index of world production shows that, during the years 1925 to 1929, the total output of primary goods rose by about 11 per cent, while it is calculated that industrial production in the principal industrial countries, excluding Soviet Russia, increased by 23 to 24 per cent, and, including that country, by perhaps 27 per cent. ¹ When the world is prosperous, expansion, both of production and of trade, takes place more readily in the super-structure of manufacturing production; in periods of depression the world is forced back to a simpler organisation based more directly upon the primary raw materials and foodstuffs.

There is, therefore, a general tendency in the trade statistics of most countries for the value of finished manufactures, imported and exported, to gain relatively to the value of raw materials. Examination of the trade statistics of individual countries bears out this conclusion.

The exports of France, Germany, the United Kingdom and the United States of America in 1929 represented over 40 per cent of the total value of world exports. When the trade between those countries is deducted, their remaining exports amount roughly to three-sevenths of the imports of the rest of the world. In the United Kingdom, the proportion of finished manufactures to the *quantum* of total exports remained stable, while, in France and Germany, it increased greatly in the post-war period. In 1910 to 1914, finished manufactures contributed 30.7 per cent of the total value of exports from the United States; in 1926 to 1930, they contributed 45.4 per cent. So large an increase in the value must reflect an increased *quantum* of manufactured exports. Since the total exports from these countries represented so large a share of the imports of the rest of the world, it is obvious that, in those imports, finished manufactures played a larger part. This is not inconsistent with the import statistics even of such countries as the British Dominions, which are themselves developing manufacturing industries. ²

Since, therefore, the imports of the raw-material producing countries continue to consist primarily of finished manufactures

¹ *Ibid.*

² The proportion of manufactured goods in the value of the total imports varied as follows:

	Percentage		Percentage
Canada	{ 1914 68.9	New Zealand	{ 1913 69.7
	{ 1930 69.2		{ 1929 80.9
Australia	{ 1913 76.2	South Africa	{ 1910-14 72.8
	{ 1928-29 76.7		{ 1925-29 78.2

and, on the other hand, the imports of the industrial countries tend to show a reduced proportion of raw materials and a higher proportion of finished manufactures, there is strong evidence of a change in the character of world trade. The statistics quoted for France, Germany and the United Kingdom leave no doubt of the tendency in those countries. In the United States of America, the case is not so clear. The proportion of raw materials in the total value of imports showed a tendency to increase after the war till about 1925, but has since fallen below the 1925 level. There is evidence also of some tendency towards increasing imports of raw materials in such countries as China and Japan where manufacturing industry is at earlier stages of development. But these conflicting tendencies can hardly compensate for the gradual narrowing of the raw-material markets in the great industrial countries of Europe. It is probable therefore that the commodity composition of world trade has been changing, the exchange of raw materials for finished products being supplemented in increasing measure by the exchange of different sorts of finished and semi-finished manufactures. This tendency has obvious limits, but it goes far to undermine the organisation of world trade which was based upon the theory that Western Europe was "the workshop of the world".

Such a tendency, moreover, accords well with other known facts of world trade. The United Kingdom, up till 1931-32 the most important free-trade country of the world, even before the war, and still more during the war and post-war period, lost ground in world trade relatively to other countries. Those countries which gained most, relatively, in world markets — the United States of America and Japan — are strongly protectionist. The United States' exports of crude materials dropped in value from 33.5 per cent. of her total exports in 1910 to 1914 to 24.4 per cent in 1926 to 1930, while, in the same period, exports of finished manufactures rose from 30.7 to 45.4 per cent of the total. The imports of raw materials into the United States for a time gained (in value) relatively to the total, but tropical products bulked large among them. Even if the United States should continue to import large quantities of raw materials, this represents an important shift in the current of world trade and does not directly compensate for the difficulty of exchanging European manufactures for the raw materials of the southern hemisphere.

In the British Dominions, Canada, Australia, New Zealand and South Africa, the exports of foodstuffs increased but those of raw materials decreased relatively to the total exports and there was a definite increase in the proportion of exports of manufactured goods which, however, except for Canada, remained small.

Trade between the various European countries tends, as industrial progress spreads from country to country, to take the form more and more of exchanges of specialised finished products, and it is significant that, in the earlier part of the depression, it was inter-European trade which, on the whole, suffered least. The sustained activity in inter-European trade during 1930 and much of 1931 was due partly to the fact that the effects of the depression were felt later in the industrial countries. A high level of consumption was maintained as real wages were increased by the fall in prices and barter terms of trade were improved for the industrial countries. There was also a substantial increase in the exchange of certain agricultural products (meat and dairy produce) between the European countries after the middle of 1929. In the long run, however, a prolonged industrial depression inevitably leads to a shrinkage in the interchange of consumers' goods, and this is becoming apparent in 1932.

When all these facts are considered together, it seems probable that, in the post-war world, the commodity composition of international trade is changing in a very important way. The industrial hegemony of Western Europe is passing and the falling export trade of the United Kingdom is merely the most striking manifestation of this general tendency. The diffusion of manufacturing equipment and technical knowledge leading to industrial development in hitherto backward countries, together with the reluctance of powerful industrial creditor countries to sacrifice their agricultural industries in order to admit cheap foodstuffs, is leading to the gradual narrowing of markets for the great export surpluses of the agricultural countries. While this tendency has not destroyed nor even reduced international trade in the bulky raw-material commodities, it has made the terms of trade less favourable for those countries which depend upon such exports and also for the great mercantile and *entrepôt* nations such as the United Kingdom. Moreover, the fact that coal shipments are now less important as return cargoes tends to make more difficult the transport of the bulky raw materials. The fact that the tramp steamer tends to disappear and be replaced by the liner emphasises the change that is under way.

A very important corollary of these changes lies in the relation of world trade to world production. It is often asserted that trade has not kept pace with production and that restrictions on international trade are among the chief causes of the present depression.

It is not easy to find a basis for this contention in the available statistics. The trend of development in the war and post-war period has not been uniform and, in any case, the period is probably too short to establish a general trend. Statistical material is,

however, more abundant since the war and some interesting deductions may be drawn from it.

The total value of the foreign trade of a large number of countries representing between 80 per cent and 90 per cent of the total value of world trade is available both for the pre-war and post-war periods. For the years after 1913, it is possible to utilise import and export price series in many countries to calculate changes in the *quantum* as distinct from the value of world trade.¹ Such series of import and export prices are not available for the pre-war period, but it is possible to utilise Sauerbeck's well-known index for calculations which yield roughly comparable results when applied to the world as a whole.

For the year 1913 and the years since 1923, there are indices of world production of foodstuffs and raw materials which, supplemented by national indices of industrial production, may be used as a guide to changes in the value of production as a whole.

If the war and post-war period is considered as a whole, there appears to be some evidence that trade has not kept pace with production. The relevant statistics are shown in the following table :

World Production and Trade 1913 to 1929.

	Index 1913 = 100 1929	Percentage increase annual average 1913 to 1929
<i>Quantum</i> of world trade . .	127	1.51
World production index of foodstuffs and raw materials	132	1.75 ²

This table, however, covers a period of great economic confusion. It is perhaps legitimate to conclude from it that, as compared with the pre-war period, trade had, by 1929, barely recovered relatively to production. It is, on the other hand, an important fact that the setback to international trade occurred in the war years, and in the depression of 1920 and 1921. During the war, there was no doubt of the failure of world trade to keep pace with production. A slight recovery in 1919 was followed by a severe slump which severely reduced both production and trade.

In the years following 1921, there was steady progress and trade recovered relatively to production. The *quantum* of commodities traded increased appreciably faster than the *quantum* of commodities produced. Statistics are more adequate after 1925 and the following table shows the development quite clearly.

¹ *Memorandum on World Trade and Balances of Payment, 1913 to 1927, Vol. I, page 11.*

² 1925 and 1929 values combined.

World Production and Trade 1925 to 1929.

	Production		Trade	
	Index : 1925=100 1929	Percentage increase (annual average) 1925 to 1929	Index : 1925=100 1929	Percentage increase (annual average) 1925 to 1929
Quantum of Primary Goods	111	2.7	115	3.6
Quantum of Manufactured Goods	127	6.7	132	7.2

A rough calculation for the three decades preceding the war would appear to indicate that the rate of increase of world trade during those years was, if anything, slightly greater than the rate of increase of world production.

World Production and Trade 1881-1885 to 1909-1913.

	Index : 1881-85 = 100 1909-13	Percentage increase (annual average) 1881-85 to 1909-13
Quantum of World Trade : ¹		
Imports	240	3.17
Exports	244	3.24
World Production Index (<i>Quantum</i>) : ²		
Raw Materials	330	4.36
Foodstuffs	167	1.86
Total	212	2.72

Caution is needed in the interpretation of these rough estimates. In particular, it has not been possible in the earlier period to obtain statistics of the trade in the different classes of commodities. For the years 1925 to 1929, it is clear that trade increased faster than production in both primary and manufactured goods. For the pre-war period, aggregate estimates only are possible. These tend to show that trade increased rather faster than production on the whole.

The indices used, however, are built up from statistics of the production of raw materials and foodstuffs. Manufacturing production should be added to obtain a fair picture of the growth of total production and if, as in the post-war period, manufacturing production was correlated rather with the raw-material index than with that of food production, it is possible that the

¹ Calculated on the base of the value of world trade for 33 countries (*cf.* WAGEMANN : " Struktur und Rhythmus der Weltwirtschaft ") and on wholesale-price movements (Sauerbeck's Index).

² Calculated as shown in Appendix II.

estimate given above (2.72 per cent) understates the average annual increase of total production.¹

There is some evidence also that in the pre-war period the manufacture of foodstuffs was relatively much more important. As a typical example, the statistics for Belgium show that the proportion of total production provided by the foodstuff industries fell from 49 per cent in 1846 to 34 per cent in 1896 and 15 per cent in 1926.

It is probable, therefore that the rate of increase in total production was less before than after the war and that the preceding table indicates with rough accuracy the relative movements of production and trade.

The remarkable fact emerges from these measurements, however, that the *quantum* of trade in the world as a whole (and also the *quantum* of production) increased very much faster in the years immediately preceding the depression than in the pre-war period and that, in the years 1925 to 1929, there was a substantially greater increase of world trade than of world production. This suggests very strongly that, in so far as restrictions upon foreign trade were in fact a cause of the depression that set in after 1925, their effects were more subtle and indirect than is commonly supposed.

Such a rapid expansion both of production and of trade, and particularly of the latter, is characteristic of periods of boom activity. The years preceding the crisis of 1907 may be cited as showing a similar tendency. It is probable that the marked improvement of trade (as well as production) in 1925 to 1929 was only partly due to the healthy development based upon European reconstruction, and that, in part, it was caused by the credit expansion which made possible a large increase in foreign borrowing in those years. In this, as in so many other ways, credit expansion temporarily covered up an unsound situation.

The fact remains that, during this period, trade did increase very fast despite the tariff barriers that were raised with increasing force. As will be shown later², however, the most important of these tariffs did not come into existence till fairly late in the period. There can be no doubt of their effectiveness in hampering the settlement of international balances from 1929 onwards. Even before that year, it is probable that they made the situation of many countries more difficult both by their effect on the

¹ The well-known estimates compiled by Mr. Carl Snyder for the Federal Reserve Bank of New York indicate a rate of increase in world production of foodstuffs and raw materials of 3.1 to 3.2 per cent in the forty years 1873 to 1913. The lower figure given above is mainly the result of including a larger proportion of foodstuffs (especially certain grains) which are not included in Mr. Snyder's calculations for the earlier decades before 1900.

² Chapter X.

barter terms of trade and by dislocating established relationships. The agricultural countries of Europe in particular suffered from the constant raising of agricultural tariffs in important European industrial countries after 1925. But, as long as international lending continued on a large scale, the balancing of international accounts was facilitated, and it was not until such lending began to diminish that the full effect of tariff barriers was exerted.

(ii) INTERNATIONAL TRADE DURING THE DEPRESSION.

The argument of the preceding section may be summarised in the statement that world trade, after the war, failed to keep pace with world production, except when supported by excessive and indiscreet capital exports. Moreover, there was an unusual degree of change in the commodity composition, as well as the direction of world trade. In this, as in other respects, the apparent prosperity, especially of the years 1925 to 1929, was based upon a credit expansion which contained within itself the seeds of its own destruction. The rapid increase of world trade in this period was caused mainly by a recovery in European trade based upon loan and credit policies that covered up fundamental weaknesses in the economic structure. The burden of debt incurred, added to already existing financial obligations, rapidly built up interest commitments, which were met by further borrowing. When this borrowing was no longer possible, the balances of trade were dislocated. Readjustment of these balances was hampered by inflexible price-structures and restrictions on international trade. The inevitable result was a deflation of export prices which soon caused the real burden of debt obligations to exceed the increased productivity resulting from the loan expenditure, if, indeed, these interest burdens were not already excessive before the fall of prices set in. The purchase of imports on such a large scale and the payment of interest were possible only as long as new loans could be raised.

The collapse of world trade after the credit expansion broke down is clear evidence that the fundamental causes of international maladjustment had not been remedied in the period of apparent prosperity. Various aspects of the situation created when the boom ended in late 1929 have already been dealt with. Prices declined heavily, especially in the case of raw materials and generally of the export surpluses necessary to meet the balances of payments. As will be seen from the table below, the *quantum* of world trade was sustained fairly well during the early part of 1930. The plight of the debtor countries was such that, in many of them, an increased quantity of goods was released for international trade, but prices

fell so heavily that the total value of world trade decreased by about 19 per cent in 1930. In the following year, added restrictive forces came into play, so that the *quantum* of trade diminished further by about 23 per cent and prices also declined so that the total value fell to still lower levels.

World Trade and Production 1929 to 1931.

	Average			
	1925-29	1929	1930	1931 ¹
Value of world trade	100	104.5	84.5	(60) ¹
<i>Quantum</i> of world trade	100	110	101.5	(74) ¹
World production :				
Foodstuffs ²	100	103	101	99
Raw materials ²	100	111	101	91
Raw materials and foodstuffs ²	100	106	101	96
Industrial production ³	100	112	97	84

The calculation of the *quantum* of world trade is a laborious process, not completed for 1931 at the moment of writing. Preliminary rough estimates, however, give an index for the value of world trade in 1931 as 60, and a *quantum* index of 74.

The magnitude of the fall in world trade which these figures represent is better appreciated if the actual values are shown, as in the following table :

World Imports and Exports 1928-1931. ⁴

\$(000,000's)

	Imports	Exports	Total Trade
1928.	30,420	28,071	58,491
1929.	31,198	28,487	59,685
1930.	25,370	22,825	48,195
1931.	18,258	16,221	34,479

¹ Preliminary estimates.
² League of Nations *Index of World Production*.
³ *Index of World Industrial Production* (twelve industrial countries, excluding U.S.S.R.).
⁴ The difference between the estimates of imports and exports is caused mainly by the fact that imports are calculated by most countries at landed value (c.i.f.) and exports at shipment value (f.o.b.). Estimates for forty-five principal countries, representing about 90 per cent of total value of world trade.

The very heavy fall in the value of world trade is seen even more clearly when monthly figures are taken extending into the early months of 1932. The trade of about forty-five countries, representing about 90 per cent of world trade, declined between the early months of 1929 and the corresponding months of 1932 in the following proportions: ¹

	Imports		Exports		Total Trade	
	1929	1932	1929	1932	1929	1932
	(Millions of dollars)					
January	2,740	1,101	2,415	957	5,155	2,058
February	2,380	1,114	2,206	1,006	4,586	2,120
March	2,562	1,120	2,418	983	4,980	2,103
April	2,770	...	2,390	...	5,160	
May	2,705	...	2,327	...	5,032	

Such figures as these show how alarming the shrinkage of international trade has now become.

Moreover the decline is continuing, since the disequilibria between and within national price-systems have not yet been adjusted, but, on the contrary, continue to be aggravated. Superimposed upon these disequilibria is a tangle of restrictive commercial policies which is rapidly strangling what remains of world trade. A summary account of the multiplication of these restrictive measures is given later. ² They have been treated in more detail, but still summarily, in successive communications by the Secretariat to the Economic Committee of the League of Nations. ³ Not only the well-known and more or less accepted measures of tariff protection, but financial restrictions such as those aiming at the control of foreign exchange; monetary events, including the abandonment of the gold standard; and extraordinary commercial arrangements such as contingent and licence systems and monopolies have been supplemented by specific agreements for the bartering of goods and of clearing arrangements designed to equalise imports and exports between pairs of countries. In Europe, particularly since the aggravation of the financial crisis in the second half of 1931, the multiplication of these various restrictions has placed foreign trade in a strait-jacket which is constantly being laced more tightly. A mere

¹ Estimates for forty-five countries. Later figures are given in Chapter XI.

² See Chapter X.

³ "Survey of the Principal Measures adopted in regard to International Exchanges since July 1931", January 8th, 1932, document E.757, and supplements E.757 (a) (January 12th), E.757 (b) (February 1st), E.757 (c) (April 5th), and E.757 (d) (May 25th).

recapitulation of the list of measures taken, without any details of their application, would occupy many pages and the only summary that is worth making at this point is that, if the present progress is maintained, there will very soon be no uncontrolled and unregulated trade at all and little that is controlled and regulated. The various European countries have almost achieved this result already and the consequences are very plain in the disorganisation of industry and an ever-growing volume of unemployment.

It is not difficult to follow the sequence of the decline in world trade in the early stages of the depression. In 1930, the heavy fall in the prices of raw materials struck the agricultural countries, particularly those outside Europe, with special severity. Certain of them were able to increase the *quantum* of their exports, but even so the fall in prices diminished the total value. Imports to certain European countries which were able to increase the *quantum* of their exports (Denmark, Lithuania, Russia, Yugoslavia and the Irish Free State) were relatively well sustained and, since trade between the European countries themselves was not so badly affected in 1930, the total trade of European countries did not diminish greatly till 1931. In the later stages of the depression, however, the reduced purchasing power of the agricultural countries in all parts of the world caused a fall in the exports of the industrial countries so that the decline in trade became general.

From the second half of 1931 onwards, the sequence of events becomes so confused that it is not possible to state anything more than that there was a general decline proceeding at uneven pace and distorted by a variety of restrictive measures. The earlier tendency was for debtor countries to restrict their imports more heavily than their exports decreased in order to obtain a stronger active trade balance, and for creditor countries to find their exports decreasing faster than their imports. This tendency is now obscured by the cumulative effect of trade restrictions and currency disturbances, so that transfer difficulties tend to be aggravated in many cases. It is difficult to make comparisons, since the abandonment or restriction of the gold standard has led to fluctuating exchange rates, but the table below shows how unevenly the values of imports and exports have diminished in various countries.

Percentage Decline in the Value of Imports and Exports of Certain Countries from January 1930 to January 1932.

	Imports		Exports			Imports		Exports	
Spain	62	71	Germany	66	49	66	49		
Hungary	59	70	Canada	60	48	60	48		
Yugoslavia	59	65	South Africa	48	47	48	47		
United States	58	64	United Kingdom	39	47	39	47		
Czechoslovakia	48	61	Italy	51	46	51	46		
Poland	63	57	Roumania	61	43	61	43		
Austria	36	54	Belgium	50	40	50	40		
Japan	37	53	Sweden	26	33	26	33		
France	51	51	Argentina	53	31	53	31		
New Zealand	49	50	Brazil	45	21	45	21		
Switzerland	21	50							

There is one further aspect of the decline of world trade which may perhaps be illustrated, but cannot as yet be measured. The distortion of the normal trade relations is indicated by the figures showing the *quantum* of various classes of goods imported into, and exported from, the three countries for which statistics are available. ¹ Not only have the total exports and imports of the three countries fallen unevenly, but there is a considerable difference in the classes of goods which show the greatest declines. It is evident that the depression has disorganised world markets to an extraordinary degree.

¹ The statistics for France, Germany and the United Kingdom which are comparable for the same country in different years but not from one country to another are as follows :

	France			Germany			United Kingdom		
	1929	1930	1931	1929	1930	1931	1929	1930	1931
Quantum of Imports									
Food	100	105	139	100*	91*	77*	100	101	110
Raw materials	100	103	91	100	91	79	100	90	84
Manufactured goods	100	125	117	100	85	67	100	100	102
Total	100	108	106	100	90	76	100	98	100
Quantum of Exports									
Food	100	106	80	100*	85*	84*	100	94	78
Raw materials	100	93	82	100	93	72	100	84	69
Manufactured goods	100	86	73	100	96	88	100	80	59
Total	100	89	76	100	95	87	100	82	62

* Excluding living animals.

The currency disturbances and trade restrictions which have complicated the course of trade since the latter part of 1931 may serve in some cases to improve or prejudice the relative trading position of individual countries, but their cumulative and combined effect has been greatly to diminish the total value of world trade. Even for those countries whose competitive position has been improved by a lowering of export relatively to import prices, there is little consolation in securing a somewhat larger share of a constantly diminishing total.

For the world as a whole, the shrinkage of world trade clearly means impoverishment. It is already reflected in increased unemployment, lowered standards of living and disorganised industry and commerce. If it should continue, the peoples of the world must forego the advantages of specialisation and exchange and suffer still further lowering of their standards of living.

(iii) THE DISTRIBUTION OF WORLD TRADE.

Detailed statistics of international trade can be assembled only after a considerable lapse of time. The collection of information concerning the items of import and export and the distribution of trade between the various countries cannot be made as quickly as estimates of the total value of trade. Such detailed information for the great majority of countries in the world in the year 1931 will not become available at Geneva till towards the end of the current year, 1932. In the meantime, it is possible to make only general observations concerning the main trends in the direction of world trade during the depression.

There are indications, however, that the depression has not only caused a startling diminution of world trade as a whole, but has also aggravated the pronounced tendency since 1925 for trade with and between the new developing countries to lag behind the average.

Attention was drawn in the first chapter of this Survey to the fact that, despite a virtual stoppage of oversea migration population was increasing fastest in such areas as South America, the Pacific slopes of North America, Indonesia, Australia and New Zealand. In these areas, production, both of raw materials and of finished products, was also increasing rapidly, new shipping routes were being established and international trade was developing so fast that, as late as 1927, it could be said, with reference to the statistics of the previous year, that "trade was passing from the Atlantic to the Pacific". Such a trend was in harmony, not only with the increasing population, but also with the rapid industrial development both of North America and of such countries as India, China and Japan.

In the years after 1925, however, the share of Europe and Africa in the world's trade constantly increased, while the shares of Latin America, Asia, Australia and New Zealand fell off considerably, and that of North America less considerably but perceptibly.

Percentage Distribution of the Value of World Trade by Continental Groups.

Continental Groups	Imports			Exports		
	1925	1928	1930	1925	1928	1930
Europe, excluding U. S. S. R.	54.6	54.9	56.8	44.3	45.8	50.3
Europe, including U. S. S. R.	55.9	56.2	58.7	45.3	47.0	52.4
North America	15.5	15.5	14.5	19.8	19.9	17.8
Latin America	7.5	7.2	6.6	9.2	9.7	7.9
Africa	4.1	4.6	5.1	4.3	4.7	4.7
Asia	14.0	13.8	12.8	18.1	15.7	14.3
Oceania	3.0	2.7	2.3	3.3	3.0	2.9

The steadily increasing share of Africa in world trade is due primarily to the rapid economic development of European — and particularly the French — colonies, mainly in Northern and Central Africa,¹ for which there has been no lack of capital throughout the whole period and which may almost be regarded as the counterpart of the industrial development of the parent countries.

The growth of European trade since 1925 was, in part, caused by a recovery of industrial and agricultural production after the war destruction and disorganisation. In so far as it reflected a vigorous restoration of economic life, it was a healthy development creating a larger total of world trade by which the share of non-European countries tended to be reduced in relative but not absolute amount.

The emergence once again of Russia as a trading country, while subject to somewhat special qualifications, should be included as part of the general recovery of European trade. In the years 1928 to 1930, Russian exports of grain, timber, mineral oils and similar raw materials again appeared on world markets, not, indeed, in quantities greater than in pre-war times, but after the world had become used to the disappearance of such competition, and accompanied by unusual trading arrangements. Under the Soviet system of planned economy, foreign trade is a State monopoly and its conduct is subordinated to the

¹ See successive issues of the *Review of World Trade*, especially that for 1929, page 20.

general line of economic policy, the main aim of which is rapid industrial development. In order to secure the capital equipment necessary for such rapid industrial progress as was called for by the Five-Year Plan, it was necessary to secure foreign exchange by mobilising for export all the resources that could possibly be assembled. Not only Soviet, but foreign statisticians also, regard this necessity as a passing phase in the economic development of the new Russia,¹ but it so happened that the re-appearance of substantial Russian exports of raw materials coincided with increasing difficulties on the part of rival producers of those commodities in other countries.

The main reasons for those difficulties have already been outlined. The restoration of European production, in itself a very desirable and healthy development, was accompanied, in its later stages, by a remarkable volume of borrowing made possible by credit expansion. The boom thus created masked the necessity for fundamental political and economic measures of readjustment to the changed post-war situation of world trade and production.

In the crisis and depression which followed this credit expansion and diversion of capital resources, the raw-material producing countries of the world suffered heavily, first because the prices of raw materials fell earlier and further than those of finished goods,² and then because there was a progressive closing of markets and strangulation of world trade. Not the least unfortunate result of the depression, therefore, has been its effect upon those countries which were the growing points of world trade. Those countries with rich natural resources, agricultural and mineral, under-equipped and not fully organised, many of them as yet lightly populated, which were growing fastest in wealth and therefore offering the most promising markets for trade expansion, were the first to be crippled when there was a block in the circulation, first of investment capital and then of international trade. The restoration of that circulation is necessary before the economic organism can again function and grow in a healthy manner.

(iv) THE TERMS OF TRADE.

There are two elements in the very heavy fall in the value of world trade. Prices have fallen and the *quantum* of goods exchanged has also been reduced. In the world as a whole, the *quantum* of world trade fell by something over 8 per cent in 1930, but, in 1931, the fall from the levels of 1929 exceeded 25 per cent.

¹ See, e.g., "Russia as a Producer and Exporter of Wheat", "Wheat Studies", Vol. VIII, No. 7, Stanford University, 1932.

² See Chapter IV.

The fall in the actual quantities of goods exchanged was unevenly distributed among the various countries and, since export and import prices have diverged so widely during the depression, it is not statistically accurate to compute *quantum* indices on the basis of any world price-index. The statistics of the individual countries need separate consideration, but it is broadly true that in the agricultural countries exports are relatively well sustained but at low prices, while imports have fallen heavily in quantity and less in price. The contrary is true of industrial countries.

More detailed examination of these facts for particular countries is contained in the annual reviews of world trade published by the League of Nations. The latest review¹ contains diagrams which show clearly that the terms of trade, as measured by the relation of export prices to import prices, have become much less favourable to the agricultural countries since 1928. Further attention will be given to this aspect of the depression in the following chapter of this Survey. At this point, it is necessary only to state the facts the significance of which will be further examined later. The diagrams reproduced in Chapter VI may conveniently be supplemented by that on the following page, showing export prices as a percentage of import prices, quarter by quarter, in three groups of countries.²

¹ Cf. *Review of World Trade, 1930* (Series of League of Nations Publications 1931.II.A.28.I), page 52.

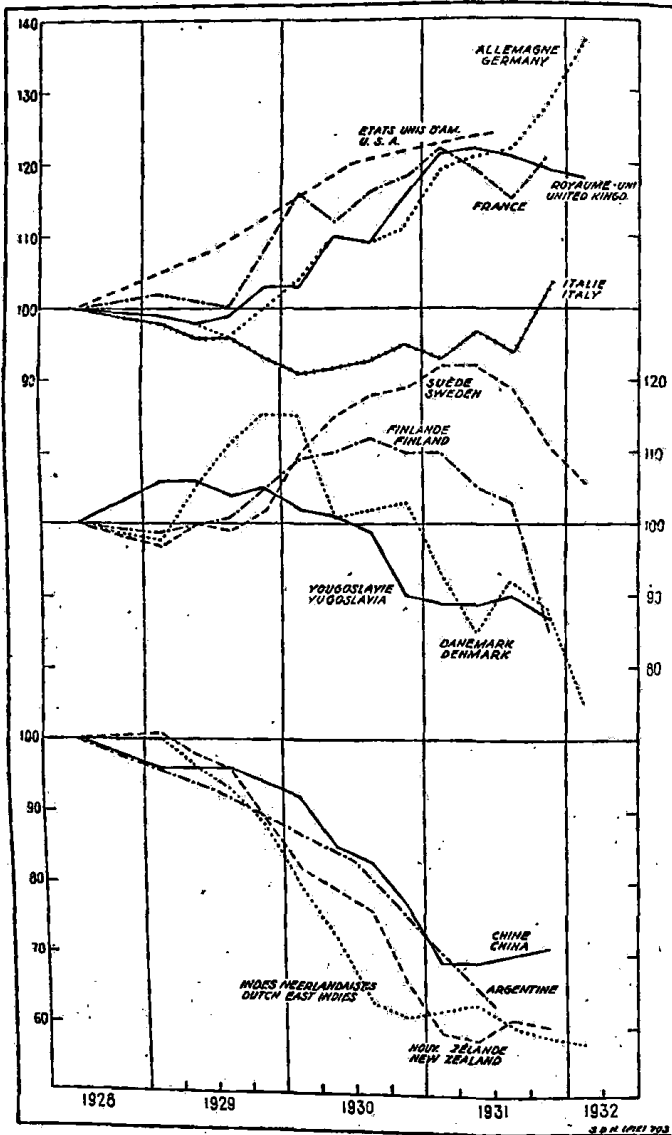
² See *Memorandum on International Trade and Balances of Payments, 1927 to 1929*. Vol. I, Summary Table III, pages 94 to 109, for a detailed description of the price-index numbers used. In the list of sources given below, those index numbers which are calculated by means of weights changed annually in accordance with the commodity composition of the trade are distinguished by the letter A. Those in which a constant system of weighting is used are lettered B. The former are much less sensitive, since, in addition to price fluctuations, they reflect the adjustment of commodity trade to changing prices.

Sources :

- I. France : *Bulletin de la Statistique Générale de la France* (trimestriel). A.
- Germany : *Monatliche Nachweise der Auswärtigen Handel Deutschlands*. A.
- United States of America : *Trade Information Bulletin*, No. 791. A.
- United Kingdom : *Board of Trade Journal*. A.
- II. Denmark : *Statistiske Efterretninger*. A.
- Finland : *Monthly Bulletin*, Bank of Finland. A. Indices of the Board of Customs.
- Italy : *Bullettini dei Prezzi*, Indices of the Confederazione Generale Fucista dell'Industria. A.
- Sweden : *Index*, Svenska Handelsbankens Indices. B.
- Yugoslavia : *Bulletin of the National Bank*. A.
- III. Argentine : *El Comercio Exterio, Argentina*. A.
- China : *Shanghai Market Prices Report*, Shanghai. Indices, National Tariff Commission. B.
- Dutch East Indies : *Prijzen en Indexcijfers in Nederlandsch Indie*. B.
- New Zealand : *Monthly Abstracts of Statistics*.
Index of Imports. B.
Index of Exports. A.
- South Africa : *Monthly Bulletin of Union Statistics*. A.
Official Year-Book.

Index Numbers of Export Prices expressed as a Percentage of Import Prices.

(Base : 1928 = 100.)



When the diagram rises, it indicates that export prices have increased relatively to import prices; when it falls, it indicates that export prices have fallen relatively to import prices.

The first group consists of countries whose exports are mainly manufactured goods, the second of European countries whose main exports are either animal products produced by methods which resemble manufacturing in their dependence upon agricultural raw materials (*e.g.*, Denmark) or whose exports consist of products (such as timber and wood-pulp) the prices of which were strongly controlled in 1930. The third group comprises some typical raw-material producing countries.

The terms of trade of the manufacturing countries became more favourable with falling prices, while those of the third group were adversely affected. For a time, the second group drew an advantage from the relatively greater fall in the prices of their imported cereal raw materials than in the prices of their finished products or from their sustained export prices. The position that arose is well illustrated by the following calculation made by the Danish Statistical Office.

	Price of butter when the price of oil-cake = 100	Price of bacon when the price of maize = 100
1928.	1,370	772
1929.	1,430	956
1930.	1,509	1,119
1931.	1,628	1,001
1931: 1st quarter	1,666	1,040
2nd quarter	1,488	1,046
3rd quarter	1,744	1,162
4th quarter	1,624	792

Source : *Statistiske Efterretninger*, January 6th, 1932.

There was a marked tendency in 1931 for the ratio of import to export prices to become stabilised in the raw-material producing countries. It is as yet too soon to discover whether this apparently hopeful tendency reflects a real and permanent improvement in the situation. In certain of these countries, determined efforts at cost reduction have been made and, in so far as these efforts are successful, they enable the countries concerned to adjust themselves to their less advantageous terms of trade.

The abandonment of the gold standard by the United Kingdom brought some measure of relief to many of these countries by reducing the burden of their external payments in so far as these were in terms of sterling. There was some recovery of

export prices immediately in terms of sterling, but the aggravated fall of gold prices which ensued checked this upward price movement so that their trading terms remain difficult.

There is a tendency for stocks to pile up¹ and the progressive restrictions which have been placed upon imports into European countries since July 1931 have further narrowed world markets, so that the terms of trade are apparently turning against the raw-material producing countries still more. A readjustment of their trading situation must be an essential preliminary step to the restoration of world trade and production, but no such improvement can take place while trade is so hampered and restricted in their import markets.

(v) THE EFFECT OF CAPITAL MOVEMENTS ON WORLD TRADE.

In the following chapter, attention is drawn to the abnormal difficulties that have arisen during the depression period in balancing international accounts. Erratic movements of capital have been largely responsible for these difficulties and there is an intricate connection between interest rates, capital movements, relative price changes and commodity trade. The action and reaction between these various phenomena has been further complicated by political, economic and financial insecurity and failure of confidence. Moreover, the movements, particularly of short-term capital, which in the boom period proved to be the active disturbing factor, were unco-ordinated. Borrowing was in many cases rendered too easy because of the possibility of raising loans from independent sources, so that weak debtors were able often to secure a series of loans from different creditors. Unwieldy financial institutions, surrounded by a complexity of subsidiary and auxiliary institutions, the intricate relations of which were all but impossible to comprehend and control, built up a labyrinth of expanded credit. International credit operations were extended and multiplied before the organisation and controls, which the narrower experience of national economic life had shown to be necessary, had been adapted to the international sphere.²

It has already been argued that the restriction of international lending in 1928-29, following a period of free borrowing, and increasing interest burdens was one of the major causes of falling

¹ Cf. London and Cambridge Economic Service, Special Memorandum, No. 32.

² Cf. O. M. W. Sprague : " Statistical Data on Foreign or Short-Term Funds : Their Collection and Use. " Meeting of Representatives of Central Banks participating in the Bank for International Settlements, Basle, May 10th, 1932 : Papers Submitted.

commodity prices.¹ In the next chapter an attempt will be made to trace some of the effects of this reversal of capital movements upon the balances of international payment, the course of prices, and interest rates. At this point, attention is directed to the simple fact that the stoppage of capital exports to the debtor countries was a powerful factor in creating the situation which has resulted in the drastic diminution of international trade that the world has experienced in the depression.

When the great creditor countries reduce their exports of capital, the very fact of reduction creates a situation in which all their debtors must meet their obligations either in goods or in gold, instead of by fresh borrowing. A strain is immediately placed upon the credit systems of the debtor countries. A deflation of prices is imposed upon them, the terms of trade become less advantageous, imports are restricted by lower purchasing power and exports are stimulated. If the financial situation becomes acute, these economic reactions may be supplemented by Government intervention — for example, by restrictions on imports or by domestic retrenchment. The net effect of the curtailment of capital imports is therefore a strong pressure to provide an active export balance in commodity trade. The strain on the credit structure is such that gold tends to be exported also, and, if the pressure continues, there may be an actual export of capital by sales of securities and similar means.

All of these phenomena were in evidence in many debtor countries in 1929, but the collapse of the American Stock Exchange boom in October of that year made credit conditions easier, particularly in the London money market, for a few months in early 1930. As prices continued to fall, however, the risks of lending became greater. New issues of foreign loans in the chief capital markets fell to such low levels that there was on balance a considerable net export of capital from debtor to creditor countries in 1931. The United Kingdom, for example, had a very substantial net inflow of capital in 1931, while France increased her net imports very substantially and the net exports from the United States of America were probably very small.

Before this extraordinary situation had fully developed, however, a further check was imposed upon the capacity of the debtor countries to pay their external obligations. The increased export surpluses which they placed upon world markets caused concern in the importing creditor countries, which thereupon imposed higher tariffs and supplemented them by additional restrictions on imports. Most of the creditor countries found

¹ See Chapter 1, section (viii).

their commodity trade balance becoming substantially more passive or less active. By the beginning of 1932, however, the creditor countries had become unanimous in refusing to receive payment from their debtors in the only form by which it was possible for the debtors to pay.

There ensued in consequence an enormous shrinkage in world trade, and the logical consequence of this shrinkage has been a series of moratoria, suspensions of payment, and standstill agreements, as a result of which the credit of many debtor countries has been gravely impaired.

The extent to which this process has gone may be judged from the diagrams which show the percentage yields upon the price of gilt-edged securities in various countries during the depression period. Increasing yield reflects the lower price of these fixed interest bonds and therefore measures the market estimation of the risks of loss. For a large group of debtor countries, the divorce of sterling from gold has alleviated their burden of external debt to the extent to which the debt was reckoned in sterling or in the currency of other countries which abandoned the gold standard. This relief has, however, been far from universal, and, since the export markets continue to narrow, there are many countries which, in the spring of 1932, in spite of moratoria and exchange controls, face the alternative of further reducing imports (and lowering domestic prices) or of currency depreciation. As early as January 1932, ominous defaults occurred upon what were even a few months before regarded as sound external loans.¹ It is plainly evident that a total value of international trade less than one-half of what it was in 1929 (and still shrinking fast) is quite incompatible with the payment of international financial obligations on the scale that exists at present. National and individual bankruptcies and repudiations of debt on a vaster scale than the world has ever seen are imminent unless international trade can once more be restored to something approaching its former freedom.

¹ For a list of loans in default up to January 1932, see *Foreign Policy Reports*, January 6th, 1932, "Recent Defaults of Government's Loans" published by the Foreign Policy Association, New York; or *Economist*, January 23rd, 1932.

Chapter VI.

THE BALANCING OF ACCOUNTS.

(i) THE MAINTENANCE OF FINANCIAL EQUILIBRIUM.

No aspect of economic discussion at the present time illustrates so well the disorganisation and confusion of economic policy and thought as the extraordinary degree of concern shown in almost every country in regard to the "balance of trade". In order to find a parallel for this universal pre-occupation, it would be necessary to go back at least to the great eighteenth century controversies between the mercantilists and their opponents. Unfortunately, however, there is, behind this revival of an ancient discussion with all its attendant misconceptions and misapprehensions, the ugly fact that the breakdown of commercial, monetary and financial organisation in recent years has been complete enough to make national economic stability a matter of deep concern to those responsible for the conduct of policy in almost every country. The fact that the elaborate and effective mechanism of international trade and finance should have broken down to so serious an extent that its erratic working has come to be regarded as a menace to national economic welfare is a measure of the destruction wrought by war and its consequences.

The balancing of international accounts in modern times is a complicated process. The classical economic maxim that exports pay for imports is almost as remote in its simplicity from the actual complexity of the financial operations involved as the earlier teaching of the mercantilists that "We must ever observe this rule: to sell more to strangers yearly than we consume of theirs in value".¹ There is an important element of truth in the maxim that imports pay for exports, but it needs to be interpreted so liberally in its application to modern problems that it ceases to have any very precise meaning.

It is easy enough to gain recognition for the so-called "invisible" items which must be reckoned with in any endeavour

¹ Thomas Mun: *England's Treasure by Forraign Trade*, 1664.

to strike a balance of payments in the international trade of any country. A glance at the estimates now published annually for an increasing number of countries will show how many and varied these invisible items are.¹ Statistics of commodities imported and exported are merely the beginning of the calculation. Shipping and commercial services, insurance, financial and other commissions, tourist expenditure, emigrants' remittances, the upkeep of governmental and commercial establishments in foreign countries, and a great number of other invisible items bear witness to the penetration of international elements into every national economic structure. China constantly imports much more than she exports, mainly because of a steady stream of remittances from her numerous and loyal citizens abroad; the United States collects cinema royalties from the whole world; Canada draws substantial revenues from royalties on hydro-electric energy generated in the Dominion but used across the border; the tourist traffic is an important factor in the economic life, not only of European countries, but also of such countries as Japan; the London Money Market, acting as banker for a large proportion of the world's trade, contributes substantial commissions towards the balancing of the British accounts.

In addition to such invisible items of import and export, there are the international movements of capital in all their variety and complexity. The difference has already been pointed out between the pre-war and the post-war organisation of the international capital market.² Long-term investments of savings gathered up in one country for the promotion of industrial enterprise in another lead ultimately to alterations in commodity trade. The capital is exported either directly in the form of capital goods, such as railroad materials, machinery and the like, or indirectly in the form of other commodities which, by a roundabout process, offset the capital expenditure that is the object of the loan. In the long run, this expenditure, if wisely made, increases the production of the borrowing country, and the capital comes home again with added interest in the form of increased commodity imports.

But this is merely the simplest form of international capital transaction, and the growing interdependence of the money-markets of the world has in recent years made possible on a vast scale movements of short-term capital such as in pre-war times were limited to temporary and infrequent occasions. It is one of the merits of the flexible modern structure of international

¹ See successive issues of the League of Nations *Memorandum on International Trade and Balances of Payments*, Volume II.

² See pages 37-45.

finance that temporary "gaps in the balance of payments" may be met by credit arrangements which avoid the necessity either of altering the ratio of commodity trade or of utilising gold for payments. The use of short-term capital transferences for this purpose gives great elasticity to the financial structure.

That elasticity, however, became a source of weakness when, because of conditions of political and economic insecurity in the years following the war, an enormous volume of short-term capital was accumulated in the principal money-markets, between which it could be, and was, transferred rapidly in large amounts either in the expectation of temporary profit or because of fears of currency instability.¹ The endeavour to find ways by which this short-term money could be invested on long-term became a major pre-occupation of the central bankers of the world.²

Into the balancing of international accounts, however, there enter other and more difficult factors than those which can be listed in an estimated balance of payments. The process of balancing consists, not of a calculation made at stated periods, but of an infinite series of day-to-day transactions into which enter, not only the quantities of commodities exchanged and the number of services rendered, but their prices; and not only the amounts of capital transferred, whether on long- or on short-term, but the rates of interest charged. The calculation made at the end of the year starts with an estimate of the total value of imports and exports, but, of the components which enter into those totals, prices are as important as quantities. The calculation proceeds with estimates of the movement of capital items and interest payments, but it is obvious that the price at which new capital has been borrowed or lent is an extremely important matter also.

There is some danger, indeed, that the static form in which the annual estimates of balances of payments are presented may obscure the essential dynamic elements of the process. In particular, there is a real risk of the conclusion being drawn that "gaps in the balance of payments" may be closed only by altering the ratio of commodity imports and exports, or — a much worse because a more enticing risk — by movements of capital. Such concentration upon the quantities of goods exchanged or amounts of capital transferred, has, in fact, only too often led to ignoring the fact that the levels of prices and rates of interest within a country are just as important factors in the balancing of international accounts as commodity trade and capital movements.

The disastrous consequences that have flowed in practice from such undue and unreal simplification, not only in popular, but

¹ *Report of the Gold Delegation of the Financial Committee, 1932*, paragraphs 47 and 48.

² *Second Annual Report of the Bank of International Settlements, Basle, 1932.*

in much expert discussion, of the problems of international trade and finance are too clearly visible at the present time to need any great emphasis. The financial structure of the world is shaken largely because of the attempt made to bridge "gaps in the balance of payments" — which in many cases were in fact unbridgeable — by the extension of fresh loans instead of by revision of the national price-levels and the provision of freer outlets for commodity trade. In that attempt, surprisingly little attention has been paid to the fact that the rates of interest at which much of the new indebtedness was incurred were so high that they ought reasonably to have been interpreted rather as danger signals than as indications of probable profit. Instead of measures being taken to reduce international financial obligations within practical limits, and then to find permanent methods of readjustment to the new equilibrium demanded, such painful necessities were evaded by the facile but superficial and temporary solution of credit expansion which for a time masked the disequilibria, but in the long run made them greater.

The balancing of international accounts, it must be repeated, is a continuous process into which enter, not only imports and exports visible and invisible, and capital movements both for long- and for short-term investment, but also interest rates and price changes. In the flexible pre-war organisation, all these elements were kept in equilibrium by the manner in which the gold standard was operated. If anything more than temporary disequilibrium developed in the financial relations of any one country with the rest of the world, an outflow of gold brought about a restriction of credit, and therefore rising interest rates, which attracted capital or checked its exportation, and falling prices which encouraged exports and checked imports till equilibrium was restored again. Such a corrective sequence of events was, however, dependent both upon a certain flexibility in the national price-structures and upon a smooth and efficient working of the standard. In the post-war world, neither of these conditions has been present, while, on the other hand, the balance of international obligations, as was pointed out in an earlier chapter,¹ demanded radical changes either in the balances of commodity trade, in relative price-levels and standards of living, or in both. There was reluctance to face the necessary changes either in the balance of trade or in the price-levels, but, on the other hand, there was rigid insistence on the financial obligations which made such changes necessary. For some years, the dilemma was evaded by a credit expansion which made possible international lending on a scale sufficient to balance the accounts for a time, but the piling up

¹ Chapter I, section (viii).

of these new obligations constantly aggravated the lack of real balance and, when the credit expansion came to an end in 1929, the "gap in the balance of payments" yawned wider than ever. As the subsequent sections of this chapter will show, the shrinkage of world trade, the confusion into which the price-structure has fallen, and the failure of confidence, which has put an almost complete stop to international lending, have in all probability now made the gap unbridgeable, unless there is a substantial scaling down of obligations.

(ii) THE BALANCE OF COMMODITY TRADE.

In the course of the depression since 1929, there have been very considerable alterations in the balances of commodity imports and exports of most countries. Attention has been drawn in a previous publication to the earlier manifestations of these changes.¹ It was there shown that from the second half of 1928 there was a noticeable tendency for the debtor countries to increase the active balance of their commodity trade, and for creditor countries to find their passive balance increasing. This was a thoroughly normal result of the shrinkage in capital exports, and of the changes in the barter terms of trade which accompanied it. There were many complicating factors, such as harvest variations; the lag, considerable in some cases, between changes in export values and in the imports ordered upon the basis of returns from previous exports; and, most important of all, divergent movements of import and export prices. Many of the agricultural countries in the southern hemisphere from time to time find themselves faced with heavy imports at high prices after the preceding high prices and increased *quantums* of their exports have been succeeded by lower values. In such cases, adjustment of the balance of commodity trade can be effected only with some difficulty and after a considerable lapse of time.

In the present depression, prices, particularly of the commodities which form the bulk of the exports from such agricultural debtor communities, have fallen so fast and so far that it has proved impossible for them in most cases to restrict their imports and expand their exports sufficiently quickly to restore the balance of trade. There arose in 1931, therefore, "a question whether it is possible for the debtor countries exporting food and raw materials to adjust their trade balance at a time when the prices of their main products are falling rapidly in relation to those of the goods forming the bulk of their imports, and when,

¹ *The Course and Phases of the World Economic Depression*, pages 211 to 214. Cf. also the annual volumes on *Balances of Payments*.

simultaneously, the state of the capital market leads to a curtailment of their foreign borrowing or even to an outflow of capital to creditor countries".¹

When these lines were written in the autumn of 1931, it had already become clear that insufficient adjustment had, in fact, been made and that this "entailed or foreboded a suspension of the payments due on account of foreign debts", thus precipitating an international financial crisis.

The main outlines of that financial crisis have already been traced.² The progressive deterioration of international trade during the winter and spring of 1931-32 rendered still more difficult the provision of external debt payments by means of active export balances of commodity trade. The movements of these balances in two representative groups of countries, creditors and debtors, is shown in the table below.

Net Balance of Commodity Trade.

(+ Excess of exports over imports; — excess of imports over exports.)

	1929		1930		1931		1931	1932
	Jan.- June	July- Dec.	Jan.- June	July- Dec.	Jan.- June	July- Dec.	Jan.- Feb.	Jan.- Feb.
<i>Debtors :</i>	\$ (000,000's)							
Argentine . . .	+112	— 26	+ 31	+ 71	+ 28	+ 47	+ 4	+ 21
Australia . . .	+ 16	—122	— 41	+ 23	+ 94	+ 53	+ 21	+ 28
Austria . . .	— 72	— 79	— 66	— 87	— 61	— 59	— 21	— 19
Germany ³ . . .	—154	— 19	+ 32	+191	+170	+414	+ 29	+ 41
India	+131	+132	+116	+ 99	+ 35	+ 61	+ 14	+ 13
New Zealand	+ 66	— 39	+ 33	— 26	+ 42	— 1	+ 7	+ 11
<i>Creditors :</i>								
Belgium . . .	— 35	— 55	— 85	— 17	— 22	— 3	— 9	— 7
France . . .	—236	— 97	—164	—209	—274	—190	—100	— 46
Netherlands	—143	—163	—158	—123	—126	—109	— 41	— 38
Switzerland ⁴	— 56	— 73	— 73	—103	— 76	— 98	— 24	— 32
United Kingdom.	—903	—965	—909	—974	—892	—935	—282	—209
United States . .	+347	+471	+223	+439	+190	+ 93	+107	+ 37

¹ *The Course and Phases of the World Economic Depression*, pages 211 to 214. Cf. also the annual volumes on *Balances of Payments*.

² See Chapter II.

³ Excluding Reparations in kind.

⁴ Including bullion.

The movements disclosed in this table are very illuminating. It is clear that the debtor countries, despite falling prices for their exports, managed in the years 1930 and 1931 to augment their active balances very remarkably. This was done mainly by drastic restrictions on imports. Australia, for example, converted a passive balance of \$44 million in 1929 to an active balance of \$152 million in 1931; Germany, in the same years, increased her active balance from \$12 million to \$694 million. These movements are all the more remarkable, since the year 1929 saw a very great change in the same direction. It is evident, however, that some of the debtor countries found difficulty in achieving this result. In New Zealand, the active balance decreased in 1930, while India's active balance was very much lower in 1931.

All the creditor countries shown in the table, with the exception of the Netherlands, found their passive balances increasing up to the end of 1931, though the increase was slight in the case of the United Kingdom. The position of the United States is most striking, since it was the only great creditor country which at the same time had a large active balance of commodity trade. In the depression, this active balance has fallen very heavily, from \$818 million in 1929 to \$283 million in 1931, and is still falling in the early months of 1932.

The comparison shown in the last two columns of the table indicates that the increase of active balances from the debtor countries continued in the early months of 1932, but that the further restrictions on imports imposed by many of the European creditor countries were reducing their passive balances. This development is marked, for example, in the case of France. The British passive balance also declined heavily. Further pressure is therefore imposed upon the active export balance of commodity trade in the United States.

These figures offer convincing reasons why, in despite of moratoria and standstill agreements, many debtor countries stand in the early summer of 1932 on the verge of further financial difficulties. There have been defaults even on loans, such as those contracted under League auspices, which were deemed to be as secure and sound as financial skill and experience could guarantee. If the deterioration of trade should continue, there would seem little possibility of avoiding wholesale default on a scale which will make reconstruction in the future exceedingly difficult.

On the other hand, in many European debtor countries, currency stability, with all its implications, is maintained, sometimes nominally, only by the most drastic controls of international trade and financial transactions. These have the effect of still further restricting trade and thus widen the gaps in the balance

of payments. They cannot be regarded as permanent solutions of the problem.¹

(iii) THE CIRCULATION OF CAPITAL.

The part played by capital movements in precipitating the fall in prices and the ensuing depression has already been discussed.² The very irregular and confused movements both of long- and of short-term capital in the years 1930 and 1931 are treated in another publication of the Economic Intelligence Service, where estimates of the balance of payment are given in as great detail as is available, and as far as possible by a uniform method, for thirty-two different countries.³ The majority of these estimates are official, but, in the case of certain countries, private compilations are employed. Together, they provide a mass of valuable information concerning the main items that enter into the balances of payment. From them it is possible to gain a fairly clear indication of the movement of tourist expenditure, shipping receipts, emigrants' remittances and a great number of similar invisible items of import and export. A complete survey of this material would be equivalent to a discussion of the international financial position of each country for which information is given.

Attention may be drawn, however, to the very marked shrinkage of invisible imports and exports, which must be reckoned with, as well as the shrinkage of international trade discussed in the previous chapter. A few illustrative examples may serve to show the magnitude of this decrease. These examples refer to the year 1930, and there is unfortunately every reason to believe that they would be more striking in 1931. The United Kingdom in 1930 was faced with a fall in her net shipping income from £130 million to £105 million; the estimated net income from overseas investments fell from £250 million to £220 million and the estimated net receipts from short interest and commissions from

¹ Cf. "The Application of Foreign Exchange Restrictions and their Effect on General Economic Conditions", by Dr. Victor Kienböck, in *Papers Submitted to the Meeting of Representatives of Central Banks participating in the Bank for International Settlements*, May 10th, 1932, especially the final conclusion: "Foreign exchange control, as we now know it, is powerless to bring about a permanent economic recovery. It is a conglomeration of police measures which are held to be necessary at a time when the flight of capital and credit withdrawals are the order of the day. As confidence returns, these measures will gradually become superfluous. But a return of confidence, which must be observed internationally, can only come about if the great problems are solved and not evaded".

² See Chapter I, section (viii).

³ *Balances of Payment, 1930* (including "An Analysis of Capital Movements in 1931").

£65 million to £55 million. In the same year, immigrants' remittances from the United States fell from \$247 million to \$199 million and tourist expenditures overseas from \$534 million to \$489 million. The very much heavier decreases in these and similar items in 1931 must be borne in mind in any consideration of the balance of payments. The provisional British figures for 1931 are net national shipping income, £80 million; net income from overseas investments, £165 million; net receipts from short interest and commissions, £30 million.

The most important items in the balance of payments outside the totals of commodity trade are, however, those of capital movements. Their importance lies, not only in their magnitude, but also in the influence which they exert upon credit and prices. In the publication to which reference has already been made, there is a fuller discussion of the statistics of capital movement in 1930 and 1931 than is possible here; but it is necessary at this point to summarise briefly the outstanding facts.

Concerning long-term investments in this period, fullest information is available for new issues of capital on the principal money markets of the world. There has been a striking diminution of such issues on foreign account since the year 1928. Information is available for four of the main creditor countries — the United States of America, the United Kingdom, Holland and Switzerland — which may be summarised in the following table :

New Capital Issues on Foreign Account in the United States of America, the United Kingdom, Holland and Switzerland.

	\$ (000,000's)
1927	2,419
1928	2,143
1929	1,284
1930	1,706
1931	512

The foreign issues in France, which are not strictly comparable with the others, were estimated at \$23 million in 1928, \$43 million in 1929 and \$55 million in 1930,¹ amounts which, while increasing, do not compensate for the striking reduction in overseas investment on the part of the other creditor countries.

Moreover, the tabular statement above does not reveal all the facts, since there have been marked changes both in the proportions of different types of loans and in the shares of the total taken by different countries. The first change may be illustrated from the statistics of lending for foreign account in the United States :

¹ Not including issues for the account of French overseas territories.

Bonds and Notes :	1927	1928	1929	1930	1931
(a) Government and municipal loans	827	586	121	548	41
(b) Industrial bonds and notes . . .	699	625	473	419	213

Shares :

(a) Preference shares	17	40	114	13	—
(b) Ordinary shares .	18	69	51	29	—
Totals	1,561	1,320	759	1,009	254

The change in geographical distribution may be illustrated by the following table :

Issues for foreign account in	\$ (000,000's)						Total	
	Europe	Asia and Oceania	Africa	Canada and New-found-land	Latin America	Issues not specified		
U.S.A.	1927	577	164	—	237	359	—	1,337
	1928	598	137	—	185	331	—	1,251
	1929	142	58	—	295	176	—	671
	1930	233	62	—	281	199	—	905
	1931	78	28	—	127	1	¹ 130	234
U.K.	1927	105	238	136	34	126	35	674
	1928	164	232	80	98	96	28	698
	1929	105	139	51	74	78	12	459
	1930	53	195	129	17	101	34	529
	1931	14	125	36	6	26	2	209

The most remarkable feature of this table is the virtual stoppage in 1931 of American lending to foreign countries other than Canada. The issues floated in the United States in 1931 for the account of Europe were on behalf of two American concerns; the issues for Asia only two, one for a Japanese, the other for a Hawaiian enterprise.

British lending in the depression was mainly to India and Ceylon, the share of those countries in the total foreign issues rising from 5 per cent in 1928 to 49 per cent in 1931. The share of other British countries (taken as a whole) fell, mainly because of the steady reduction of Australian borrowing.

Of the French issues for foreign account an increasing share appears to have been absorbed by Poland, Czechoslovakia, Hungary, Roumania and Yugoslavia.

¹ International issues.

Further analysis of the very marked drop in the total of foreign investments, therefore, emphasises the alarming extent to which there has been a stoppage of long-term investments. For long-term capital movements in 1931, other than new issues, detailed information is not yet available, but even in 1930 new direct investments in foreign business were falling rapidly. Direct new investments in foreign business enterprises by citizens of the United States, for example, were estimated in 1928 at \$378 million, but this figure fell in 1929 to \$335 million, and in 1930 to \$253 million. Available figures for the trade in already existing securities disclose an import rather than an export of capital by the great creditor countries. In 1928 and 1929, the United States recorded net purchases of foreign securities amounting to \$105 million and \$169 million respectively, but, in 1930, there was a net sale amounting to \$446 million. While American citizens were getting rid of their foreign securities in this way, in Germany there was a net purchase. Capital, it is evident, was flowing uphill, from the debtor to the creditor countries.

When attention is turned to the movement of short-term capital, very striking but confused changes are evident. In the years preceding the depression, the amount of short-term loan money available in the principal money markets increased very rapidly. The reasons for its accumulation are not far to seek and allusion has already been made to them.¹ It has been estimated that the total amount of short-term international indebtedness which existed at the beginning of 1931 aggregated more than 50 milliard Swiss francs (c. \$10,000 million).² The central banks of the world were increasingly concerned with the menace to currency stability such large amounts of short-term holdings represented. In the first half of 1931, indeed, the "essential emphasis" of the work of the Bank for International Settlements "was laid upon the necessity, if imminent dangers were to be lessened, of reducing the quantity of short-term credit in the international markets and of its transformation into more permanent capital."³

The violent movements of short-term capital in the depression period have depended only in part upon economic and financial forces. Political insecurity leading to fear of currency instability has been a prime factor, and the chronicle of short-term lending in the depression years gives evidence of the irregularity and magnitude of the movements that were caused in this way. For example, "the gold reserves and foreign assets of the Reichsbank fell by 855 million marks in June and 112 million marks in July

¹ See Chapter I, section (viii), and Chapter II, section (i).

² Bank for International Settlements: Second Annual Report, May 1932, page 11.

³ *Ibid.*, page 7.

(1931)", and, later, "of the total amount of foreign (largely French) capital invested on short-term in the United Kingdom — according to the Macmillan Report, about £400 million — about half is estimated to have been withdrawn between the middle of July and September 21st (1931)".¹ Available statistics for individual countries show clearly how great and irregular the movements were. The statistics for the United States, for example, show an inward balance of \$179 million in 1927 which gave place in 1928 to an outward balance of \$386 million. The stock exchange boom attracted short-term credit in 1929, so that there was an inward balance again that year of \$24 million, followed in 1930 by an outward balance of \$334 million.

In an earlier chapter, the complication of the inward and outward movements which resulted in such variations of the net balances was illustrated by reproducing the details of Germany's balance-sheet in this respect.² There was a constant fluctuation of lending and repayment in various forms.

The undertone of the movement, however, was the continued movement from 1928 onward of short-term balances back to France, and their reinforcement by flights of capital and speculative operations as currency instability threatened in many countries after the middle of 1930. In the last three months of 1931, there set in a further heavy movement, accompanied, as in the case of the French balances, by gold shipments, to several other European countries which held large foreign assets. The reduction of foreign short-term holdings of European central banks and the accompanying increase of their gold reserves is shown clearly in the following table :

Central Bank of :	Unit (000,000's)	Gold Reserve		Foreign assets ³	
		End of 1930	End of 1931	End of 1930	End of 1931
Belgium	Belg. fr.	6,862	12,749	4,852	0
Bulgaria	Leva	1,455	1,511	793	257
Czechoslovakia	Kč.	1,545	1,650	2,447	1,060
France	French fr.	53,578	68,863	26,204	21,500
Italy	Lire	7,081	7,399	4,327	2,170
Netherlands . .	Gulden	426	887	247	86
Roumania . . .	Lei	9,275	9,675	1,822	323
Switzerland. . .	Swiss fr.	713	2,347	438	103

¹ Memorandum on Trade and Balances of Payments, 1930, Volume II.

² Chapter II, section (iv).

³ As shown in the published returns, which, however, do not in all cases disclose total foreign assets and liabilities.

In one important respect, the continued liquidation of short-term holdings of foreign assets, which began with the repatriation of French balances in the latter part of 1928 and was strongly reinforced after the widespread abandonment of the gold standard in the latter part of 1931, has contributed to aggravating the financial depression. During the earlier period, from 1921 to 1928, the money markets of the world had become used to a continuous increase in the amount of such short-term credits. The existence of these credits helped to support the boom in the United States and also to support British lending on long and short term. Credits to Germany, and at one remove to Soviet Russia, were facilitated by the continued augmentation of short-term money in the lending markets. All through the period, from 1925 to 1929, this process went on and, as the short-term credit found its way to the final borrower, an increasing proportion of it was in fact tied up in medium- and long-term investments.

After the French short-term balances began to return to Paris in increasing amount from the latter half of 1928, the basis for much of the credit expansion was withdrawn, and when, after the break of the Stock Exchange boom in October 1929, and the subsequent aggravation of the fall in prices, financial difficulties became acute in the debtor countries, confusing cross-currents of short-term capital movement arose. Political and psychological as well as economic factors were at work. In the first half of 1930, there was a temporary revival of long-term lending including some conversion of short-term loans, but, as the investigations of the German financial position previously referred to have shown,¹ a considerable flight of capital took place in the second half of the year, and endangered the currency stability, not only of Germany, but of other European countries also.

Towards the middle of 1931, there was a marked aggravation of financial strain. The events which moved rapidly from crisis to crisis between the months of May, when the Oesterreichische Creditanstalt difficulties became known, and September, when the United Kingdom abandoned the gold standard, have already been summarised.² During these months, short-term capital movements were decidedly away from the threatened debtor countries³ to the stronger creditor countries. International action, for the most part mobilised by and through the Bank for International Settlements, stemmed the flow to some extent by arranging short-term credits to support the threatened central

¹ See Chapter II, sections (iii) and (iv).

² *Ibid.*, *loc. cit.*

³ The United Kingdom was a debtor on short-term account, but not on long-term.

banks,¹ but the continuance of the crisis created the necessity of negotiating a series of standstill agreements and moratoria in the latter months of 1931 and the beginning of 1932.

The net result of all these confused movements of short-term capital has, however, been a considerable drain from the weaker countries, which has reinforced the net effect of the stoppage of long-term lending. Statistics are not yet available for most countries, but provisional estimates for Germany and Great Britain in 1931, as disclosed in the following table, show how much greater the drain of capital back to the creditor countries has been in that year than in the preceding year.

*Inward (+) or Outward (—) Capital Balance in Millions of Dollars as calculated indirectly from the Trade in Goods, Services and Gold.*²

	1927	1928	1929	1930	1931
U. S. A.	— 580	— 1,099	— 206	— 196 ³	
United Kingdom ⁴	— 385	— 569	— 574	— 112	+ 340
France ⁵	— 504	— 237	+ 20	+ 252	
Germany	+ 1,072	+ 1,007	+ 553	+ 148	— 500 ³

(iv) MOVEMENTS OF CAPITAL, INTEREST RATES AND PRICES.

In the preceding section of this chapter and in earlier chapters of this survey,⁶ attention has been drawn to the irregularity of capital movements as a cause of instability in the post-war period and of increasing financial stringency in the depression. Such capital movements, however, derive their importance from their relation to the price-structure of the various countries concerned. The major irregularity in this movement, which was aggravated by the fact that the proportion of short-term to long-term loans tended constantly to increase, is to be found in the sudden reversal of its direction in 1928-29, after a prolonged period of expanded lending based upon credit inflation. Both in the period of expanded lending and in the depression years

¹ Cf. Bank for International Settlements: Second Annual Report, Basle, 1932.
² Memorandum on International Trade and Balances of Payments, 1930, Volume II.

³ Preliminary estimate.
⁴ Excluding Government capital transactions.
⁵ Excluding amortisation of inter-allied debts. The territory considered includes the French overseas territories, except Indo-China.
⁶ See especially Chapter I, section (viii).

when capital was drawn back again to the creditor countries, it was the relation of such capital movements to price changes, both as effect and as cause, which was important.

The connection between the supply of capital and the prices of commodities is maintained through the complex structure of interest rates. The connection is not simple, but depends upon the fact that the supply of bank credit is the medium by which capital is made available and by which also the production of goods and services is distributed. Bank credit forms, as it were, a liquid fund, into which the major part of national productive effort is poured and from which are drawn the streams of goods for consumption and of capital for further production. But this fund may be temporarily swollen or diminished by banking policy expressed through changes in interest rates and open-market operations. The amount of bank credit made available and the rates of interest paid on the one hand to those who forgo their claims to consumption and therefore accumulate savings, and charged on the other to various classes of borrowers, largely determine the division of total production between consumption and various capital uses, and, in determining it, go far to influence the ratios at which the various kinds of goods and services are exchanged. In other words, the ruling rates of interest not only affect the proportions of the total production of goods and services which are respectively saved and consumed, but, in doing so, influence the relative prices of those goods and services.

The various rates of interest are themselves the resultant not only of the supply of capital but of the demand for it in different directions. There is not one interest rate in the money market but several, and the demand which makes itself felt in regard to each of these rates is a composite demand built up of the need for capital in a variety of directions. Thus the rate of interest on industrial advances is determined in part by credit policy, but in part also by the massed demands of various forms of industrial production. Moreover, in a developed money market, there are as many interest rates as there are classes of loans, each of them representing the composite demand of different types of borrowers who find that particular form of loan suitable to their needs. The money market, with its different and fluctuating rates of interest and discount, is constantly in a state of shifting equilibrium as between the different types of borrowers and the different classes of loan money made available.

In the determination of interest rates, therefore, many more forces than the purely monetary considerations connected with the supply of available credit are operative. All the varied

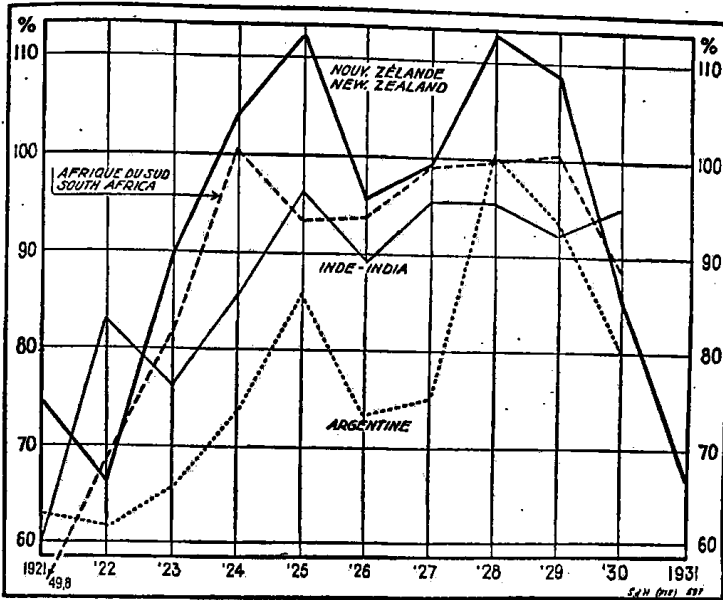
factors which determine industrial activity, including commodity prices, are summed up in the different demands for credit and therefore influence, at the same time as they are influenced by, interest rates. For this reason, the master-rate of interest, the rate at which the Central Bank in a fully developed money market will discount the most liquid bank paper, may at times have but nominal influence upon or relation to the other rates of interest ruling in the market. The supply of credit is largely determined by the bank rate, but the demand for it is not, and the market rate of interest represents the price at which demand is equated to supply. The market itself, affected by the varied factors of demand for credit which are, temporarily at least, independent of its supply, may prove unresponsive to changes in the master-rate. The control of central banking authorities in the principal creditor countries — the ultimate arbiters of the supply of credit — while always potentially, and for the most part practically, powerful in determining market interest rates, and through them prices, is, therefore, neither absolute nor unvarying. Credit conditions in the borrowing countries are largely dependent upon the lending money markets.

Movements of capital, whether on short or on long term therefore, in so far as they are governed by economic causes, are the visible result of an extremely complicated action and reaction between interest rates and relative price-levels in more than one country. To describe their irregularity as causes of instability either in the price or in the credit structure of any country or of the world as a whole is merely an elliptical way of drawing attention to disharmonies in the price and interest systems of the various countries concerned. To leave the statement there, thus concentrating attention solely upon the effect of such movements would be to ignore their causes and thus mistake a description of symptoms for diagnosis.

The irregularity of capital movements in recent years, however, has not been wholly dependent upon economic causes. Political factors have played a part, and at times a large part, in creating conditions of economic insecurity or fears of policies leading to economic insecurity, which have caused capital movements against the apparent pull of economic factors. Thus, in the depression, high rates of interest have not been able to prevent flights of capital to monetary centres where rates have been consistently low. Capital has sought the safest refuge rather than the highest remuneration. Indeed, it might be argued, political policies arising largely from the war have played a large part in creating the economic conditions analysed below as mainly responsible for the direction of capital movements in recent years.

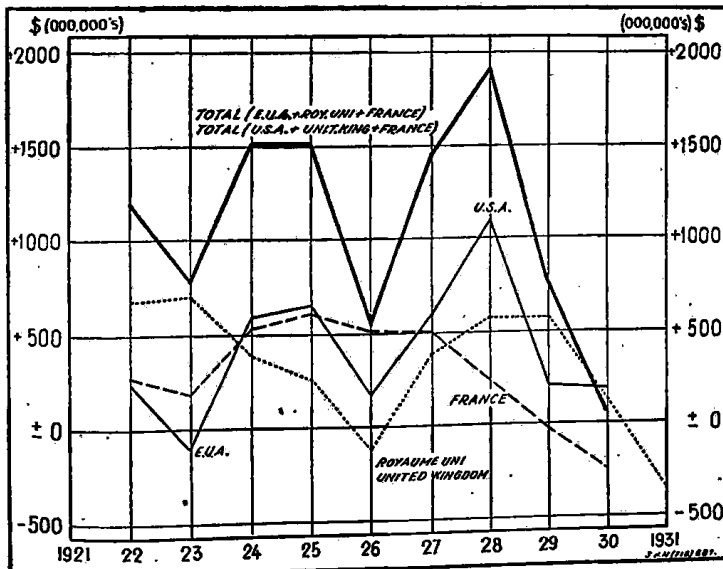
Export price index as percentage of import price index of certain countries exporting raw materials and foodstuffs (Argentine, India¹, New Zealand and the Union of South Africa²).

Source : Review of World Trade, 1930.



Net capital exports (measured indirectly as the balance on account of goods, services and gold) of the United States of America, the United Kingdom³ and France⁴.

Source : Balances of Payments 1930, League of Nations.



¹ India : years beginning April 1st.

² Union of South Africa : merchandise only.

³ United Kingdom : private capital operations only.

⁴ France : including French overseas territories (with the exception of Indo-China); excluding amortisation of inter-Allied debts.

The financial situation after the war and immediate post-war inflation was extremely difficult. Even after the worst of the inflation was over and the great majority of countries had returned to the gold standard in one form or another, there were grave maladjustments in the economic structure, and political and psychological as well as economic difficulties in setting them right. The first chapter of this survey was devoted to a summary outline of the more significant of these maladjustments and in the final section of that chapter it was argued that the necessity for facing the difficulties they presented both to creditor and to debtor countries was temporarily masked by large transferences of capital which were made possible by the period of credit expansion, particularly from 1925-1929. The very large capital movements of these years were made possible by, and in turn contributed to maintaining, relations between the national price-levels and standards of living in debtor as compared with creditor countries which were not in fact consistent with the financial obligations that had been incurred and the rearrangement of productive organisation that had resulted from the war and the peace settlement.

The relation that exists between the capital movements of this period and price-changes has been demonstrated in another publication of the Economic Intelligence Service of the League.¹ It has there been shown that the terms of trade of a series of borrowing countries varied coincidentally with the fluctuations in the exports of capital from the major lending countries. The diagrams in which this coincidence of movement is shown are reproduced above. It is not contended that such a coincidence is proof of causal connection between the two phenomena.² The intricacy of the reactions between interest rates and price levels is too complex for any simple and direct sequence of causation to be demonstrated. But it is significant that the greatest amounts of capital export and the movements of prices favourable to the debtor countries occurred in the years of rapid credit expansion based upon cheap money policies.

The following diagram shows the close connection between capital exports, price movements, industrial production and gold movements in the United States of America. The years in which a policy of credit expansion was followed by the Federal Reserve bankers were years of increasing capital exports followed by rising prices of raw materials and gold exports and, after a time, by increasing industrial production and rising prices of

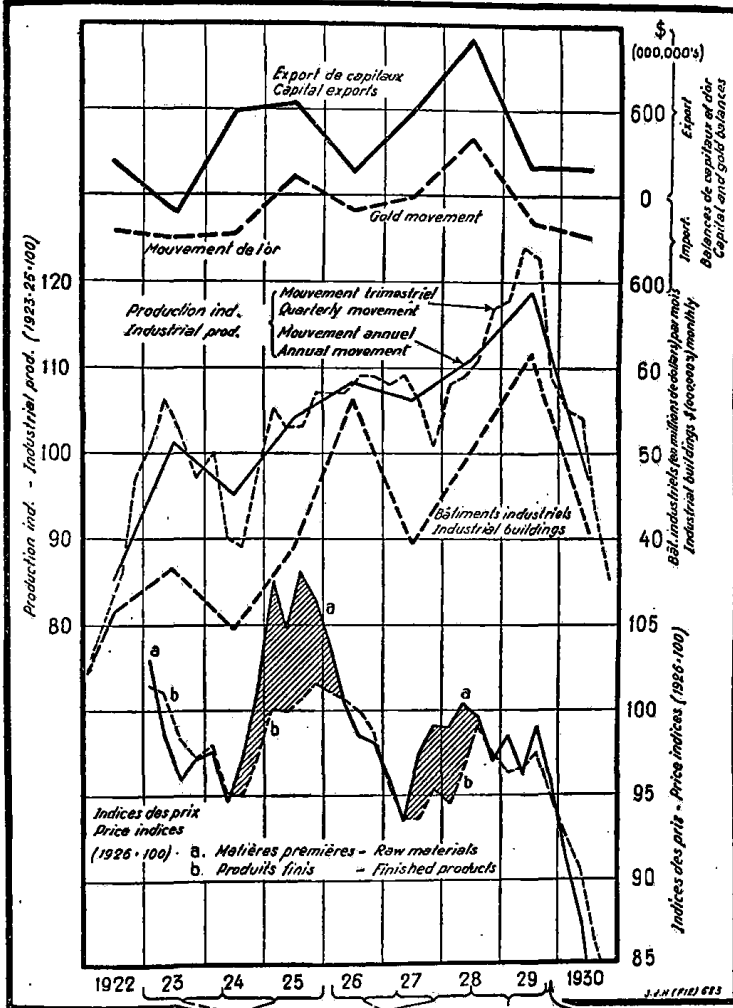
¹ *Memorandum on International Trade and Balances of Payments, 1930, Volume II.*

² *Cf., Roland Wilson: "Capital Imports and the Terms of Trade", Melbourne University Press, 1931.*

United States capital and gold movement, volume of industrial production, industrial buildings (36 States), and price indices of raw materials and finished products.

The curves for capital and gold balances and industrial buildings show the annual movement, those for price indices the quarterly movement. For industrial production, both the annual and the quarterly movements are shown.

Source (except for capital and gold balances) : *Survey of Current Business* (U. S. Dept. of Commerce).



Prices of raw materials relatively high, industrial production relatively low. Domestic investment and consumption low, but large capital exports. Gold exports (or small gold imports).

Prices of finished products relatively high, industrial production high. Domestic investment and consumption high, but capital exports reduced. Gold imports.

Definite turn of the business cycle.

finished products. There is an evident rhythm in these movements, industrial production being highest in the years of relatively low raw-material prices, of decreased capital exports and of gold imports; but external events such as the British coal strike in 1926 and the French franc stabilisation in 1927-28 exercised a disturbing influence on their relations.

It is to be remembered that these years, 1922 to 1929, were, in the United States, years of expanding credit and fairly stable commodity prices, despite a distinct tendency towards falling prices elsewhere. In the subsequent period of depression and falling prices the reversal of capital movements has exercised a strong deflationary influence in the debtor countries, which has, however, been strongly resisted, particularly in so far as it affects domestic price-levels and wage-rates. The reversal of commodity trade balances caused by falling prices has, moreover, been countered by increasingly severe restrictions on international trade.

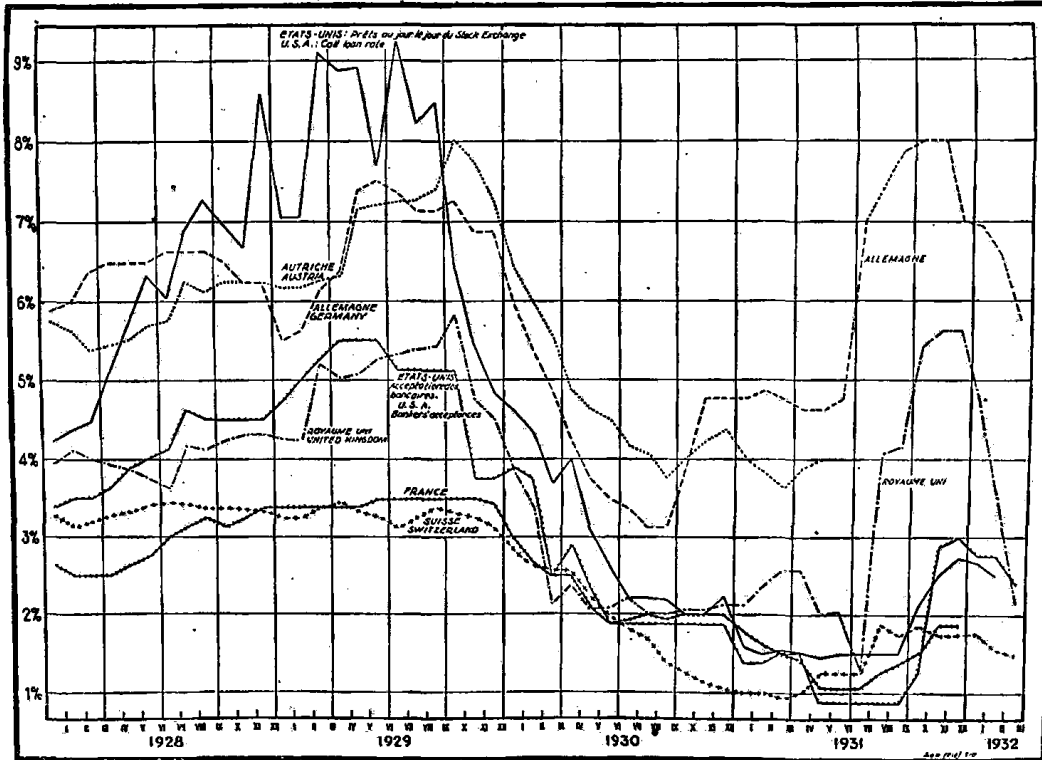
In the receiving creditor countries, an increase in the available supply of credit, coupled with low interest rates and low prices of raw materials, might be expected to stimulate industrial production.

Though at times there may, under certain conditions, be relatively high raw material prices with low interest rates, the usual reaction, leading once again to reviving prosperity and capital exports, is that suggested above. The failure of inward capital movements at the present time to evoke such a reaction is an indication of the extent to which the economic organisation is demoralised. As even the most cursory inspection of discount and interest rates will reveal, the ordinary economic stimuli are no longer fully operative. Their effect is restricted at every turn by political interference, by fear of insecurity, both political and economic, and by all the disequilibria created in the course of the depression, the correction of which is hindered by the inflexibility of a partially controlled and regulated economy. The competitive forces which would liquidate these disequilibria are prevented from doing so, and in default of their harsh but effective operation, or of any effective alternative production and trade drift in to paralysis.

The disorganisation of the capital market is very clearly reflected in the yields of bonds in lending and in borrowing countries. The data upon which the diagrams reproduced in Chapter IX are based are to be found in the *Statistical Year-Book of the League of Nations, 1931-32*, and their significance is discussed in Volume II of the *Memorandum on International Trade and Balances of Payments, 1930*.

In the main creditor countries, the price of long-term capital fell from 1929 to the middle of 1931. A precisely opposite

Market Discount Rates (minimum rates, prime commercial bills ¹) and U.S.A. Stock Exchange Call Loan Rate (average for renewals), 1928-1931.



¹ For Switzerland in 1928, the average discount rate is shown. It is only slightly higher than the minimum rate.

movement is clear in the debtor countries, where the yields of bonds rose rapidly from the middle of 1929 onwards. A temporary resumption of capital movements in the first half of 1930 brought a fall in these yields, but, from the middle of 1930, they increased again rapidly, until in the financial crisis of the latter months of 1931 they rose to alarming heights. It is clear that such yields connote risk premia, and that very grave fears of financial collapse are widespread among investors. It is noteworthy also that international loans (because of the difficulties of transfer consequent upon exchange regulations) have been more seriously affected than loans floated on the domestic markets. Throughout this period, there has been a flight of capital from the countries of high interest-rates to those where interest-rates are low and falling.

The same broad tendencies may be seen in the diagram which shows the movement of market discount rates for prime commercial bills in a group of representative countries. Since the middle of 1930, discount-rates have been high in all the debtor countries ; but the plethora of funds on the principal creditor money markets has kept rates at very low levels. Those markets which, like London and New York, were at certain periods debtors on short-term account, despite their long-term creditor position, experienced high discount-rates during those periods. Short-term capital moved in large amounts from the high discount-rates to the low. A striking example of this unusual movement was provided by the flight of capital from the United Kingdom, while the bank rate stood at $4\frac{1}{2}$ per cent and market rates ranged higher, in the months before the United Kingdom abandoned the gold standard, as contrasted with the marked return flow of short-term credits when rates were being lowered on the London market in the early months of 1932.

The paradoxical situation has been created whereby capital has fled from apparently tempting rates of interest to seek refuge where profits are low. Debtor countries are starved of capital, and its accumulation in creditor countries is such as to pass beyond the possibilities of productive use. Both politically and economically, the times are out of joint and there can be no return to the orderly circulation of the world's capital resources until confidence is restored by the settlement of outstanding political differences and the removal of restrictions upon the normal working of economic forces.

(v) THE CONCENTRATION OF GOLD RESERVES.

In the balancing of international accounts, not only commodity trade, but invisible exports and imports (including capital movements) — and, in the last resort, gold shipments — come

into play. All of these methods of payments are closely linked with alterations in the national price-levels concerned, but the two latter, capital movements and gold shipments, have a much closer relation with the credit structure and therefore with the monetary factors which affect all prices. In periods of relatively stable equilibrium, the settlement of balances is achieved in the short run by such movements of short-term credit as are necessary to bridge over any temporary deficiency or surplus in the equation of goods, services and long-term capital investment. Over a longer term, divergent interest-rates and their correlated price movements may bring about a persistent movement of long-term capital such as that which, in the second half of the nineteenth century, facilitated the development of the newer agricultural communities of the southern hemisphere.

The distribution of the world's supply of gold was part of the process of balancing accounts, an important part, since gold provided the basis upon which most monetary systems were erected ; but a minor part in times of relative stability. In the total process of settlement gold movements were as much the consequence as the cause of changes in national price-levels and interest rates. If a divergence of national price-levels proved too persistent to be corrected by the changes it stimulated in the movements of commodity trade, invisible imports and exports and short-term credits, the foreign exchange diverged from par and gold moved from the countries of higher to those of lower price-levels. Such gold shipments were in fact the signals of divergence arising between national price-levels and, upon their occurring, the monetary authorities took the requisite measures to bring pressure to bear upon interest rates so as to correct the divergence. If such signals were ignored and a persistent gold movement set in, the country losing gold was sooner or later forced off the gold standard.

In conditions of relatively stable equilibrium, therefore, gold movements were the last element in a delicately balanced and self-corrective mechanism by which national price-levels and interest rates were kept in adjustment one with another. Gold shipments were small and brought with them their own corrective consequences. The total stock of gold in the world so greatly exceeds the annual increment of new gold from the mines that the latter was readily distributed without undue disturbance of the price-levels through the principal banking centres which maintained a free gold market.

The unobtrusive ease with which gold was thus distributed, and the efficiency with which this routine and simple organisation kept the world's currency systems relatively stable and in equilibrium with each other, were fundamental conditions for the

building up of the network of international trade and finance which has contributed so greatly to increase the wealth of the world. The irregular functioning of the gold-standard system in the post-war period, culminating in its breakdown over a large part of the trading world, is at once a result of the disorganisation arising from the war and a cause of further disorganisation.

Concerning the facts of gold movements in the post-war period there is no dispute. The Gold Delegation appointed by the Financial Committee of the League has dealt exhaustively with the statistical data concerning the world's gold stocks, the supply of new gold, and its distribution.¹ After mature consideration, the Delegation recorded its opinion that "the world's total stock of monetary gold, apart from any considerations as to its distribution among different countries, has at all times in recent years been adequate to support the credit structure legitimately required by world trade and that the rapid decline in prices which began in 1929 cannot be attributed to any deficiency in the gold supply considered in this sense".

The breakdown of prices and credit, in other words, cannot be attributed to a geological accident. The supply of gold was adequate; but it was not successfully managed. What broke down in fact was the balancing of international obligations, of which gold movements have been a part, and in recent years a part of unprecedented importance.

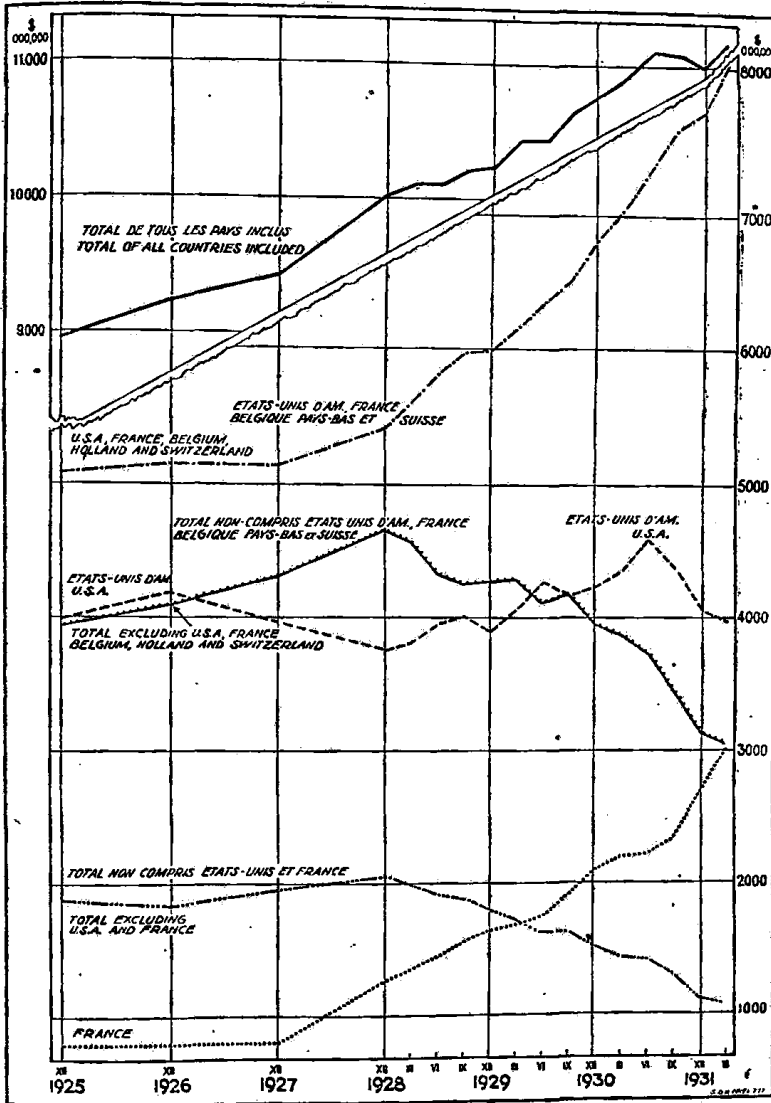
The diagram with which the Gold Delegation illustrates its discussion of the distribution of gold reserves is reproduced below in a form that is slightly altered in order to bring out more clearly the different movements in the United States of America and France.

The facts shown in the diagram are clear and can be stated summarily. Between 1925 and 1928, the period when there was a widespread return to the gold standard after the war and post-war inflation, the United States parted with substantial amounts of gold and these, with the new additions to world stocks, were sufficient to provide a remarkably steady and even increase in the gold reserves of the remaining countries of the world.

Early in 1928, however, this movement broke down. In this year the United States began to import gold again on balance, while France, to which a flow of gold had set in during the preceding year, continued to add to her gold stocks, which have increased continuously up till the moment of writing in the early summer of 1932. In the early part of 1928, as a

¹ "Report of the Gold Delegation of the Financial Committee", Geneva, May 1932; Sections IX and X, and statistical appendix. See also *Statistical Year-Book of the League of Nations*, 1931-32.

Changes in the Gold Reserves of Central Banks and Treasuries¹



¹ Including the Banco de la Nación Argentina, which, although not a bank of issue, acquired a considerable gold reserve in 1927 and 1928 in view of a proposed banking reform; practically the whole of this reserve was subsequently exported. The following countries are excluded throughout: Union of Soviet Socialist Republics, Cuba, Mexico, Central-American Republics, Paraguay, the Philippines, Straits Settlements and Turkey.

consequence of the re-import of gold into the United States and the French demand, the remaining countries of the world, with a few exceptions, began to be drained of their gold reserves, a process that, with minor fluctuations, continued until many of them had by the latter part of 1931 abandoned the gold standard and the others were only nominally and with difficulty maintaining it by imposing restrictions on their international payments. Three countries in Europe—the Netherlands, Belgium and Switzerland—were able to use their strong credit positions to safeguard, and after September 1931 to strengthen, their gold reserves; but the United Kingdom, the largest creditor country in the world on long-term, was a debtor on short-term, and abandoned the gold standard after experiencing a sustained flight of capital in the middle of 1931.

The causes of the developments thus summarily described must be sought in an analysis of the process by which international accounts were balanced first in the period before 1928, and then in subsequent years. Into that process there entered all the elements briefly described in the preceding sections of this chapter—commodity trade, capital movements, price-changes, shifts in interest-rates, as well as the gold movements, which, indeed, may be regarded as the culmination rather than the origin of the process.

The turn of events in 1927-1928 gives the clue to the primary causes of abnormally large gold shipments since that period. Two extremely important monetary decisions were taken in these months—the French currency was stabilised and, later, in the early summer of 1928, the Federal Reserve Board began to take measures to check the developing credit inflation. The stabilisation of the French franc was accomplished *de facto* in December 1926 and *de jure* in 1928 at a level which continued domestic consumption at the low level to which it had fallen during the inflation. This allowed capital export to continue during 1927 and the early part of 1928 and later gave scope for the expansion of French industry and the attraction of capital imports, since the internal value (in real purchasing power) of the franc was higher than its external value. French balances abroad built up during the previous period of currency instability—partly by the flight of French capital, partly by profits from speculation in the currency, partly by reason of the bonus on exports while the currency was depreciating—were brought home to participate in the expansion of French industry, part of them in the form of gold.

The fortuitous advantage given to France in the balancing of her international accounts by the fact that her currency was stabilised at a low level was essentially a price advantage. As

gold was attracted to France, this advantage would have been lost if the countries losing gold had curtailed their credit structures and deflated their price systems correspondingly.

Such a suggestion, however, valid as it may be in economic theory, at once raises questions of extreme practical difficulty. The European countries which had been devastated by the war had been rescued from extreme economic disorganisation by their own and international effort. It is a moot question whether the international obligations with which many of them were faced, given their curtailed resources, were in fact capable of being met. Any serious effort to have met them in the only permanent way—by the export of commodities—would have entailed drastic readjustments of the price-level and industrial organisation, not only in the debtor, but also in the creditor countries. The issue was evaded. Loans were made available and, for the time being, several unpleasant readjustments were postponed—the obligations remained in force, the creditor countries were saved the necessity of receiving disturbing payments in goods, but instead sold goods to their debtors on credit, while the latter were enabled to sustain standards of expenditure incommensurate with their real and permanent resources.

The credit expansion which made such a temporary arrangement possible was in full swing during most of the years 1925 to 1929. The even distribution of gold reserves in those years was made possible by it. Attention was drawn by the Gold Delegation to this fact in its statement that “the cheap money policies adopted by Federal Reserve Banks in those years (1924 and 1927) were intended, not only to influence the domestic situation, but also to assist the European Central Banks first to restore and then to maintain the gold standard”.¹

More than a year before the Stock Exchange boom burst in New York in October 1929, this process of supporting the price-levels and credit systems of borrowing countries by extensive issues of foreign loans was proving increasingly difficult to sustain. As credit expansion brought rising standards of living in its train, and accumulating interest burdens were increasing the strain of external payments, the first slackening of foreign loans in the middle of 1928 caused grave difficulties to the debtor countries in the balancing of their accounts. They began to lose gold which flowed mainly to France and to the United States. The loss of gold, however, was not followed by measures of credit restriction adequate to place the price-levels of the gold-losing countries once more in equilibrium with those of the

¹ Report *op. cit.*, paragraph 36.

stronger creditor countries, and so the drain continued. The receiving countries differed materially in their economic position. There was no lack of credit available in the United States during 1928-29 and the renewed inflow of gold can hardly be said to have been sterilised at this time, if ever. The large increments to her gold stock which France received were slower in making their effect felt than they might have been in other countries or under other circumstances. France had always before the war maintained a large gold reserve and there was a considerable deficit to be made up before any excess gold stock created conditions favourable for credit expansion. Moreover, the low level of stabilisation gave scope for a considerable rise both in security and in commodity prices before the domestic levels were brought into equilibrium with the external value of the franc. France was able therefore to absorb considerable amounts of gold before the usual corrective consequences stimulated rising prices and checked the gold imports.

There were signs of credit expansion and industrial activity in France in 1929, betokening the beginnings of a gold inflation ; but before this could get under way, the drain of gold from the debtor countries had proved intolerable. The processes by which they were led to such a measure of credit restriction as caused the fall in prices which was proceeding with increasing force from the middle of 1929 onwards have already been described¹. The loss of gold from their bank reserves was merely one aspect of the development.

When the fall in prices became precipitous, after the breakdown of the American inflation in October 1929, the difficulties of the debtor countries in balancing their accounts were gravely aggravated. The virtual stoppage of capital exports and the withdrawal of short-term credits further worsened their position and they lost gold steadily. The gold thus lost accumulated mainly in the reserves of less than half-a-dozen Central Banks. After the widespread abandonment of the gold standard in September 1931, there was a further stimulus to the disposal of foreign credit holdings and their encashment into gold. A "gold-rush" set in on New York, the effects of which are clearly reflected in the diagram. The following table, summarised from the report of the Gold Delegation, shows how violent this movement was :

¹ See Chapter IV, section (i).

Central Gold Reserves.

	June 30th	1931 December 31st ((\$000,000's))	1932 March 31st
France	2,211	2,683	3,010
Switzerland	162	453	471
Netherlands	200	357	353
Belgium	200	354	350
Total	2,773	3,847	4,184
United States	4,593	4,051	3,985
Rest of World (excluding U.S.S.R.)	3,756	3,123	3,067
Grand Total	11,122	11,021	11,236

Such a marked concentration of the gold reserves of the world as now exists renders the restoration of the gold standard in the near future a very difficult process for many countries. In the previous restoration of the gold standard (1923 to 1928) the accumulation of the necessary gold reserves was facilitated, not only by cheap credit policies, but also by the large foreign loans that were facilitated by such policies. In default of the renewal of such lending upon a scale that at the present time seems impossible even if it were desirable, there are but two possibilities, either the continuance of inconvertible managed paper currencies with fluctuating exchanges, or such drastic and sustained changes in relative price-levels as between creditor and debtor countries as will provide an active balance of trade by which the debtor countries may again accumulate gold reserves.

It is possible that the second alternative may take the form of a revival of the gold-exchange standard or a variant of it such as the "credit-exchange standard" practised by Australia and New Zealand, or a sterling-exchange standard. The Gold Delegation recorded its opinion that the gold-exchange standard still offers for many countries "the most economical and efficient monetary mechanism available"¹, and raised the question of its reconstruction under international auspices.

In the meantime, the continuing concentration of gold reserves into a few Central Bank reserves is evidence that the balancing of international accounts is still impossible without gold shipments. The smooth distribution of the world's gold has been disorganised as thoroughly as other aspects of the economic mechanism. Gold has reappeared from eastern hoards and in some

¹ Report, paragraph 221.

western countries also — particularly in the United Kingdom — hoarded gold has been surrendered. Between September 1931 and March 1932, an amount estimated at \$180 million was released from Indian hoards; and even earlier the collapse of the price of silver in China had led to a large gold export.¹ The industrial demand for gold also fell off, but, on the other hand, gold-hoarding developed in other European countries. The total sum hoarded in the latter half of 1931 is estimated at \$400 million, which is not far short of the world's annual production.² The net effect of these various movements was that, even though the amount of new gold coming from the mines increased substantially, the available stock of monetary gold decreased in the latter half of 1931.

The uneven distribution of the total stock remains one of the most striking symptoms of lack of balance in the international accounts. Its continued aggravation is proof that the situation is getting worse. When gold begins to flow again to the bank reserves which are at present depleted, it will be the surest sign of recovery. Before it does so, there must be adjustment of equilibrium in the national price-levels; prices must rise in the gold-holding countries relatively to the price-levels in the countries now losing gold. Trade restrictions must be lifted in order that commodity trade may be resumed. Even then, the prospect of balancing international accounts will depend upon a reasonable settlement of outstanding financial obligations and such a measure of political *rapprochement* as will make possible, not only the resumption of trade, but also the circulation of capital.

¹ Report, paragraph 122.

² *Ibid.*, paragraph 125.

Chapter VII.

BANKING AND CREDIT POLICY

(i) RESTORATION OF THE BANKING STRUCTURE AFTER THE WAR.

In the process of returning to the international gold standard after the currency disorganisation of the war period, important alterations were made in the statutes of many previously existing central banks, and many new banks with the sole right of note issue were founded.¹ It is important to realise the fact that the currency and credit mechanism which was reorganised in the first post-war decade differed in many important respects from the pre-war system. In the sphere of central banking, there was not only a larger number of central banks, but the general trend of their statutes and of the new currency legislation, except in the important matter of minimum reserve ratios, was to provide for greater elasticity in their operation.² The appearance of new institutions, or of banks of issue with powers approximating to those of central banks, implied a greater degree of national organisation of credit and currency policies, but many of these new banks served money markets which continued to be influenced largely by conditions in the principal financial centres.

Post-war central banking policy and practice became increasingly important from the years 1924 to 1926, when currency stabilisation on a gold basis was achieved in a number of important commercial countries.

Most of the new central banks were made independent of Government control. A greater degree of budgetary stability had in any case been achieved after the period of hyper-inflation and there was a considerable measure of economic recovery.

There still remained, however, a very great deal of economic maladjustment and instability, and it is essential " to recall the

¹ See successive issues of *Memorandum on Central Banks*. For a detailed analysis of the post-war developments, see KISCH and ELKIN — *Central Banks* (London, Macmillan, 1929), Appendix I of which gives a summary of Laws, Charters and Statutes regulating Banks of Issue in thirty-one countries.

² Cf. FELIKS MLYNARSKI, *The Functioning of the Gold Standard*, Geneva, League of Nations, document F.979 (F.Gold 67(1)).

fact that the working of the restored gold-standard currencies encountered difficulties of much greater novelty and magnitude than had been known in the pre-war period".¹ In its final report, the Gold Delegation of the Financial Committee of the League of Nations drew attention to some of the intractable phenomena with which the monetary and banking authorities had to grapple in this period.² The first chapter of this *Survey* has also summarised some of these difficulties. It is necessary here to refer briefly again only to the facts that, even after the depression of 1920 and 1921; the national levels of prices remained high relatively to pre-war standards, that they were not in equilibrium with each other, and that an unprecedented burden of financial obligations had been incurred at the even higher levels of prices ruling during the war period. The economic system had not only been geared to a mass of contractual obligations at a higher level of prices, but had become less flexible, so that reductions of the average price level (as distinct from the adjustment of the national price levels) obviously threatened to cause a period of economic struggle and difficulty. The world had become used, during the war, to conducting its business at higher price levels made possible by great credit expansion. Reversion to the pre-war monetary policies would necessarily have involved a contraction of credit, even beyond that which occurred in 1920 and 1921. With the evident prospect ahead of rapidly increasing commodity production, it was expected that price levels would fall, unless changes in monetary and banking policy made possible the continuance of a large volume of credit. It was for this reason that the Genoa Conference (1922) strongly urged its proposals for economising the use of gold.

There was a further important change in the post-war situation arising from the emergence of the New York money market as a greatly strengthened financial centre. Leadership in monetary policy had in great measure crossed the Atlantic. In the United States of America the Federal Reserve system, created only in 1913, had not functioned in a period of world peace. The expansive possibilities of that system were not fully tested; there had not been time to discover their implications and devise controls for them. Throughout the years 1921 to 1924, as was shown in Chapter II, the continued accumulation of gold in the United States, added to the expansive possibilities of the system itself, made for easy credit conditions which, when other countries returned to the gold standard, were capable of

¹ *Report of the Gold Delegation of the Financial Committee, League of Nations, Geneva (document C.502.M.243.1932.II.A), paragraph 42.*

² *Ibid.*, Section IV.

being communicated to them in such a way as to create a pronounced credit expansion after 1924. The large volume of foreign lending which developed was part of this process.

In the newly restored banking and currency systems a primary aim was greater elasticity in the powers of the central banks to create credit on the basis of existing gold reserves. The final report of the Gold Delegation draws attention to the major changes in this respect, both in the statutes of central banks and in the development of banking policy.

The first important change to be noticed is the widespread adoption of the gold-bullion standard in place of the pre-war system which was a compromise between the gold-circulation and the gold-bullion standards. Gold stocks were largely withdrawn from circulation and concentrated in the reserves of central banks. This not only increased the amount of gold available as a basis for credit creation, but enhanced the powers of the central banks which were no longer faced with the prospect of internal drains from their reserves into circulation, except in times of panic for hoarding as bullion.

The result of this concentration of gold stocks in the central bank reserves was to make it possible, even in the period of marked increase in the commercial bank deposits, to maintain a sufficient basis of currency to support the credit structure. The monetary supply is often described as consisting of an inverted pyramid, the apex-base of which consists of central bank gold reserves upon which are built successive layers of central bank credit, commercial bank credit and, finally, book credit. After the war, the base was both larger and more solid (in the sense of not being subject to internal drains). It was, moreover, supplemented, as will be shown later, by the holdings of foreign exchange which, in many banking systems, could be used as a basis for note issue or credit creation. The Gold Delegation recorded its opinion "that the world's stock of monetary gold, apart from any considerations as to its distribution among different countries, has at all times in recent years been adequate to support the credit structure legitimately required by world trade and that the rapid decline in prices, which began in 1929, cannot be attributed to any deficiency in the gold supply considered in this sense".¹

The adequacy of the supply of monetary gold, it should be noted, refers specifically to the period 1925 to 1929, during which credit was very greatly expanded.

The statutory checks imposed upon the creation of credit by the central banks (as distinct from the economic limitations.

¹ *Report of the Gold Delegation of the Financial Committee*, paragraph 109.

set by market conditions) consist mainly of reserve requirements. "The Bank of England stands by itself as preserving a legal freedom of action unknown elsewhere".¹ In most countries, the limitations within which the central bank operates are specifically laid down by law. After the war, most of the central banks which were created or reorganised adopted some variant of the system under which the reserve ratios to be maintained were fixed at a certain proportion of the total sight liabilities of the central bank, including notes and deposits. Thus the Banque de France after 1928 was required to maintain a reserve in gold bullion or coin amounting to 35 per cent of its notes and current accounts. The legal requirements for other central banks were fixed at different levels in accordance with the economic and financial circumstances of the countries concerned. In many cases, a provision was introduced by which the banks might allow the reserve to fall below the legal minimum upon payment of a tax, and, in some cases also, upon raising the discount rate.

The Federal Reserve Board is required to keep a 40 per cent gold cover against notes and 35 per cent gold and note cover against deposit liabilities. The ease with which credit can be created in the United States has already been discussed in connection with the development of the boom of 1925 to 1929.² It is a notable fact, however, that among the plans proposed in the United States for banking reconstruction as an aid to recovery from the depression, those which provide for greater power on the part of the banking authorities in the creation of credit take the most prominent place.³

In the same way, the Gold Delegation in its report strongly recommended the reduction of reserve ratios. This was done primarily because "this whole system of defined ratios has proved itself, in the light of the special circumstances of post-war years, to be too rigid and inadaptable". The main object of the recommendation is to "give the central banks adequate freedom and flexibility in the conduct of their credit policy".⁴

Some members of the Delegation would go even further and abolish the whole system of legal minimum ratios.⁵ These quotations offer clear evidence of the trend of expert opinion. The whole process of banking reconstruction since the war has been

¹ KISCH and ELKIN, *op. cit.*, page 13.

² Chapter II, section (i).

³ Chapter XI.

⁴ *Report of the Gold Delegation of the Financial Committee*, paragraphs 209 to 214.

⁵ *Ibid.*, page 71.

in the direction of placing greater power and more freedom in the hands of the central banks.

The elasticity introduced into the post-war banking mechanism is an elasticity upwards; the outstanding and almost the only principle of credit control (the reserve ratios) which worked in the direction of enforcing credit contraction became a subject of criticism when it began to be strongly effective. The reason for this is obvious enough in the facts stressed earlier in this section, the legacy of debts and contractual obligations and the inflexibility of the economic organisation inherited from the war period.

In practice, the statutory controls over credit expansion did not prove rigid in the post-war period until the unbalanced financial and price situation built up in the boom precipitated the fall in prices which ushered in the depression. While credit was expanding in the United States, gold became available to the borrowing countries and their banking structure was sufficiently elastic to provide as much credit as was necessary to facilitate industrial reconstruction and maintain their price structures.

The post-war period has also witnessed an advance in central bank co-operation, especially since the foundation of the Bank of International Settlements. It is clear that, quite apart from the results or lack of results over such a short period, the experimental beginnings of central bank co-operation are extremely important. They are, indeed, as the Gold Delegation pointed out, an essential element in any approach to fundamental monetary reforms. "Methods of continuous consultation and co-operative effort to maintain the international equilibrium without sacrificing national interests"¹ are as urgent a necessity in the banking as in the political sphere. Great potential importance attaches in this connection to the creation in 1930 of an international institution — the Bank of International Settlements — which, in addition to its other functions, provides a meeting-place for a great number of the world's central bankers.

The reconstruction of the banking systems since the war, therefore, has strengthened the position of the central banks in the monetary organisation and has rendered their control over national banking policies more direct and their co-operation a more practical possibility. But this is far from placing them in a position to direct economic policy generally. Greater power to control the supply of credit is only half the story. The demand for credit in practical affairs is determined by a host of economic,

¹ Report, *op. cit.*, paragraph 194.

political and social considerations, as well as by the monetary factor of its supply price, which alone is in the hands of the central bankers.

In the post-war period, the economic and financial situation was peculiarly intractable. It is theoretically conceivable that, in a purely economic world, central banking policy might have been directed to a coldly realistic appraisal of the revolutionary adjustments of prices, trade balances, and economic organisation necessary to meet the changed pattern of international indebtedness after the war, and to a ruthless application of the measures necessary to secure those adjustments. It might, however, be argued that not even the most drastic and ruthless credit contraction in the debtor countries, unless accompanied by inflation which would have proved uncontrollable in the creditor countries, could have succeeded in balancing international accounts while political insecurity, policies of economic nationalism and inflexible price systems barred the way. It is certain that such readjustments were in fact socially and politically impossible.

(ii) THE DEVELOPMENT OF CENTRAL BANK PRACTICE.

In addition to the structural changes sketched in the preceding section, there were, in the post-war period, very important developments of central banking practice. The practice of holding large balances on short term in foreign monetary centres is discussed in the following section in connection with the revival of the gold-exchange standard. In this section, it is necessary to draw attention to some of the practical expedients and particularly the increased use of open-market operations and the attempt at international co-operation, which were a logical result of the greater responsibilities of the central banks after the war. A much greater element of control or management entered into the various currency systems, involving the development or extension of central bank practices designed to influence the money markets.

The main instrument of control over currency and therefore over credit policy has always been the central bank rate of discount. As explained in Chapter VI, the alterations of this rate are of special importance in connection with the balancing of international accounts. Before the war, when gold coin circulated in most countries and the situation of the gold reserves was the dominant consideration in determining central bank policy, changes in the discount rate were generally effective in causing such alterations of the price structure as kept international accounts in steady equilibrium. Purchases or sales of

gilt-edged securities were resorted to by some central banks in order to liberate or constrict the credit resources of the commercial banks. This practice, however, was used generally to reinforce the effect of changes in the discount rate. Occasionally special circumstances made it desirable to undertake such open-market operations in opposition to the movement of the discount rate in order to smooth over essentially temporary disequilibria, which might otherwise have caused gold movements and undesirable price fluctuations.

The development of open-market operations into a major instrument of policy after the war is a significant feature of the management of currency. The circumstances which gave rise to it are to be found only partly in the monetary organisation. The increased volume of Government securities and the necessities of public finance affected the situation from time to time. The more inflexible price structure and the resistance to downward adjustments of the price level also made necessary more frequent resort to this method and, very significantly, such operations were undertaken more and more as a substitute for, or a counteraction of, changes in the discount rates. Moreover the difficulty of achieving and maintaining international equilibrium made the conservation of gold reserves in many cases peculiarly difficult, so that, by every means possible, gold movements, which in any case were very large, were minimised.

Concern over the growing instability of the credit expansion in the United States, the slowness with which, under special circumstances, the French money market reacted to the strong position on international account which it developed after stabilisation at a low level, the vulnerable position of the United Kingdom as a debtor on short term and a creditor on long term, and the rigidity of prices and wages, in addition to the growing restrictions on international trade in many countries, made the maintenance of the price level increasingly difficult after the middle of 1928. The situation has been summarised by the Gold Delegation in its discussion of the difficulty that arose early in 1928 in "reconciling the national and international factors in monetary policy".

An increasing movement of short-term credit balances back to France, largely in the form of a continuous import of gold, set in about the middle of 1928. The Federal Reserve Banks began to raise their rediscount rates "in an endeavour to check the growing speculation in the security and real estate markets". Foreign lending in the United States fell off and credit stringency began to develop in the borrowing countries. The United Kingdom, faced with a difficult situation both internally and externally, was "constantly on the economic defensive after 1925, and, unless

interest rates were kept low abroad, there was always the possibility of a drain of gold depleting the comparatively small gold reserves of the Bank of England".¹ In face of this situation, there developed a growing tendency to credit stringency which culminated in the crisis of the latter part of 1929.

(iii) THE ACCUMULATION OF SHORT-TERM FOREIGN BALANCES.

In many ways the most remarkable development of the post-war banking system has been the continuous and rapid growth of short-term credit balances. This phenomenon is practically universal, and may be regarded as a symptom of the disorganisation and insecurity of the post-war world. Credit resources have not found their way into profitable long-term industrial investment, but have, to an increasing degree, been accumulated in the principal money markets. A recent publication of the Bank of International Settlements estimated the total of such short-term holdings at the beginning of 1931 as at least \$10,000 million.

The existence of such large amounts of floating capital has proved very disturbing to the working of the currency mechanism since the war. The phenomenon known as "a flight of capital", which makes its appearance at any time of financial or currency strain, is largely created by the transference of such short-term holdings from one money market to another.

Moreover, the normal operation of the gold-standard mechanism, under which an alteration in the discount rate effects changes in the price structure, is very greatly distorted by such movements of short-term credit. If there is need for the discount rates to be raised in an effort to check the expansion of credit and so induce a tendency for prices to fall, the increased holdings of short-term credit attracted by the higher rates of interest available may nullify the change in the discount rate. The connection of gold movements with the price levels of the countries concerned has been rendered less direct and effective. This factor has been of very great importance in contributing to the inflexibility of price systems and hindering the readjustment of international price-equilibrium.

The effect of credit operations of this character in complicating the working of the gold standard in recent years has been the subject of much discussion.² It is obvious that the

¹ Report, *op. cit.*, paragraph 37.

² Cf., e.g., Dr. Feliks MLYNARSKI : *The Functioning of the Gold Standard*, League of Nations, Geneva [document F.979 (F, Gold 67(1))], and also *Report of the Gold Delegation of the Financial Committee*, paragraphs 24 to 28.

management of the gold standard has been rendered much more difficult and the consequences of the usual methods of control have become more erratic by reason of the existence of such large holdings of short-term credits as those which have been shifted between the principal money markets in recent years.

The further problem arose in the period before the depression of the use made of a portion of these short-term balances held abroad, as a basis for further credit creation. In the general fear of a scramble for gold at the beginning of the reconstruction period, provision was made in the statutes of many central banks whereby the obligation to convert their notes into gold coin was changed into an obligation to convert them into gold bullion, foreign gold-exchange or either at their option. The detailed regulations concerning the use of foreign gold-exchange in central bank reserves differed somewhat in specific cases, but the avowed object was to effect an "economy in the use of gold".

The creation, on a much wider scale than ever before, of this mechanism — the gold-exchange standard — led to a growing body of criticism in the latter stages of the boom period.

In so far as the central banks which were liable to be drained of gold by a realisation of the foreign exchange reserves of other countries took precautions not to allow their domestic credit issues to expand to the full extent made possible by their gold holdings, the danger of a double credit expansion upon the same gold stock was avoided. The net effect of the gold-exchange standard practices, however, was quite clearly to assist the credit expansion of 1925 to 1929, and indeed the system was created largely in order to economise gold.

There were other rather unexpected results of the system in the distortion of the gold-standard mechanism. The growth of foreign balances referred to above was only partly due to the new reserve legislation. The Gold Delegation estimated the aggregate amount of the floating foreign balances of central banks, or rather that proportion of the amount which could be calculated from published statements, as almost \$3,000 million at the end of 1930.¹ Not all of this total was held by countries legally on the gold-exchange standard, but, since several of the countries which had used foreign assets as additional reserves had converted a large proportion of them into gold after the abandonment of the gold standard by many countries in the latter part of 1931, the Delegation quoted the figure of \$3,000 million as an upper limit of the possible demand for gold, arising from the liquidation of the gold-exchange standard.

¹ Report, *op. cit.*, paragraph 123.

In addition to central bank reserves held abroad, there were much larger holdings of foreign short-term credit by commercial banks, and it is obvious that the counterpart of the credit expansion made possible by the accumulation of short-term credit in the years before the depression is to be found in the deflation later induced by the encashment of foreign balances. This process began in 1928 with the repatriation primarily by the commercial banks of the French balances, mainly in the form of gold.

As the deflation proceeded, the dangers, both to the banking systems in which the balances were deposited and to the depositors, became evident. The former were exposed to the risk of sudden large withdrawals which might adversely affect the liquidity of the central bank and therefore currency stability. This risk was the greater since the central bank in many cases did not have full information concerning the total short-term liability contracted by the commercial banks and the money market.¹ Those central banks, on the other hand, which held part of their reserves in foreign balances, ran the risk of those reserves being suddenly and drastically reduced by a depreciation of the currency in which they were held.

Both of these risks became actual disasters in the latter part of 1931, and the gold-exchange standard was thereby discredited. But this development was inherent, not in the simpler and more restricted use of the gold-exchange standard as it had been practised by many countries for several decades before the war, but in the undue expansion of the practices modelled upon it and in the unstable political, economic and financial situation which caused the accumulation of such a great volume of short-term credit, domestic and foreign, as was built up after the war. For this reason, the Gold Delegation stated quite clearly its belief in the gold-exchange standard, as it was practised before the war, "as a useful system for many countries, for whom it still remains the most economical and efficient monetary system available".

(iv) COMMERCIAL BANKING AFTER THE WAR.

The *Memorandum on Commercial Banks, 1913-1929*, recently published by the Economic Intelligence Service of the League of Nations, bears witness to the variety and differing stages of development of the commercial banking structure in various

¹ Report, paragraphs 26 and 204.

countries. It is clear that commercial banking in its many forms is adapted, not only to the wealth, but also to the history, legislation and commercial customs of the different peoples. Each country has its own problems of organisation. Nevertheless, it is possible to discover in the wealth of statistical information assembled in the *Memorandum*, certain tendencies of great importance which are more or less common to most of the principal banking systems.

The commercial banking situation in most countries was profoundly affected by a marked change in the proportion of capital resources to total liabilities. The following table brings out this change very clearly.

*Percentage Ratio of Banks' own Resources to their Public Liabilities, excluding Acceptances and Sundry Accounts, at the End of the Years indicated.*¹

Country	1913	1925	1929
Austria ²	33.3	17.4	15.1
Belgium ³	24.3	16.8	25.6
France ²	24.7	8.0	9.5
Germany ³	39.2	17.0	9.3
Netherlands ²	52.8	30.8	28.0
Sweden ³	32.0	19.5	19.7
Switzerland ³	21.7	16.5	15.7
England and Wales ³	10.1	7.5	7.4
Canada ³	17.5	9.4	9.8
U. S. A. ³	19.8	12.7	15.6
South Africa ^{3 4}	16.2	9.9	12.2
Australia and New Zealand ^{3 4}	22.2	18.6	20.2

There has also been a fairly general tendency for the cash ratios kept by the commercial banks to decline. The statistics for the same group of countries are set out below.

¹ *Commercial Banks, 1913-1929*, page 26.

² Principal commercial banks.

³ All commercial banks.

⁴ End of June, each year.

Cash Ratios of Commercial Banks.¹

Country	1913		1925		1929	
	I	II	I	II	I	II
Austria ²		3.2		3.4		3.6
Belgium ^{3 5}	7.4	5.7	12.0	8.6	17.2	12.5
France ^{3 6}	10.9	10.1	17.6	17.0	16.3	15.1
Germany ⁵	14.3	8.1	14.8	7.6	5.7	2.1
Netherlands ^{2 3}	13.2	7.3	14.2	7.8	13.7	6.7
Sweden ⁵	19.9	3.2	11.0	2.4	11.2	2.4
Switzerland ^{3 5}	8.9	2.1	10.3	3.1	10.1	3.0
England and Wales ⁴			20.6	11.8	19.9	10.8
Canada ⁵	31.0	13.2	40.2	13.3	28.9	10.1
U. S. A. ⁵	20.8	16.3		9.1	15.1	8.8
South Africa ⁵	31.3	17.1	25.3	14.5	21.6	11.1
Australia ^{5 7}	58.0	24.4	45.1	19.8	42.6	15.9
New Zealand ^{5 7}	34.7	18.9	21.2	12.9	21.7	10.9

There is a further significant tendency towards a general movement from shorter to longer-term deposits. For various reasons already stated, "the public has been less willing to invest directly in industrial undertakings by the purchase of shares or to lend to such undertakings in exchange for bonds; it has preferred to keep a larger proportion of its funds in liquid form".⁸ Had this movement not been accompanied by a change in the period and type of credit allowed, it might have been considered to justify some reduction in the cash ratios. But, in fact, less liquid advances were made, and the illiquidity of bank assets has in many countries proved to be a major financial weakness.

It is extremely important to bear this fact in mind when considering the growth in total deposits, especially in the period 1925 to 1929. That growth is shown in the following table.

¹ *Commercial Banks, 1913-1929*, pages 50 and 52. Column I represents the percentage ratio of the banks' holdings of coin (including bullion in a few cases), inland notes and balances with the central bank, to their short-term liabilities (demand deposits, notes and cheques in circulation). Column II represents the ratio of these items to total deposits, notes and cheques. The detailed statistics given in the *Memorandum* include also calculations based on cash thus defined and "other items of a cash nature".

² Principal commercial banks.

³ Includes "other items of a cash nature".

⁴ London clearing banks.

⁵ All commercial banks.

⁶ Principal deposit banks only.

⁷ End of June, each year.

⁸ *Commercial Banks, 1913-1929*, page 48.

*Percentage Movements of the Total Deposits of Commercial Banks
(corrected for Changes in Wholesale Prices) in Certain Countries.*¹

(1925 = 100.)

Country	1926	1927	1928	1929
Austria	128	141	152	128
Belgium	74	97	106	128
France — deposit and investment banks	109	133	161	174
Germany	140	165	187	204
Netherlands	108	111	115	122
Sweden	103	105	106	117
Switzerland	115	120	138	160
England and Wales	106	114	119	121
Canada	108	119	128	127
U. S. A.	107	120	121	122.
South Africa	117	124	134	150
Australia ²	107	110	119	124
New Zealand ²	101	101	111	120

The index numbers shown in this table represent the total deposits of the various banking systems (current accounts, sight deposits, savings and time deposits) corrected by the index number of wholesale prices at the end of each year and expressed as a percentage of the 1925 index in each case.

There are notable variations in the growth of total deposits, and it is obvious that the much greater growth in certain countries is due in fact to the reconstruction of the banking system after the devastation caused by the post-war currency depreciation, and to the attraction of foreign assets.

In certain countries where deposits increased most rapidly, the cash ratios were most heavily reduced. This exposed the banks to a strain which they could not resist when subsequently the depression, and more particularly the credit crisis, set in.

In connection with this table, there is an important observation to be made. The growth of total deposits represents an expansion of credit, but it does not necessarily represent an increase in the amount of purchasing power. The growth shown above was mainly in long-term deposits. The *Memorandum on Commercial Banks, 1913-1929*, draws attention to this fact in the following statement. "The fact that the total amount of credit outstanding

¹ *Commercial Banks, 1891-1929*, pages 30 to 35.

² End of June, each year.

has grown does not mean that the amount of effectively utilised purchasing power has been proportionately increased. The increase in credits outstanding has therefore not prevented prices from falling ; demand deposits have shrunk."

This statement invites a great deal of reflection and analysis. It calls attention to some of the major difficulties in the economic organisation of the post-war world and comes very near to the heart of the crisis. The phenomena indicated are worthy of more detailed exposition and investigation than is possible here.

In a great number of countries, the extension of business enterprise was made possible by bank advances rather than by capital subscription. The *Memorandum on Commercial Banks, 1913-1929*, sums up this tendency clearly :

" In post-war Europe, the contrast between pure deposit banking and industrial banking systems has been considerably weakened. The systems of the former type have extended their operations over a considerably wider range of activities and have entered into much closer relations with industry than formerly. This is partly the result of the first post-war depression which seriously affected many of their most important customers ; short-term credits became frozen, and, to protect their own interests, the banks were frequently obliged to take over the security for loans previously granted and to assume direct control over large industrial undertakings. The direct relationship thus established between banks and industry enabled the former to exercise an active influence on the reorganisation of the latter. The gradual liquidation of the banks' industrial engagements proceeded relatively slowly and had been only partly effected when the present depression set in. Furthermore, in some of the countries concerned, issues of industrial shares and bonds, especially those of older industries, have been less easily marketed in the past decade than formerly ; industry, accordingly, has had to rely upon bank credits to a greater extent."

Among the many reasons for this development, the tendency for taxation to fall heavily on profits derived from large-scale business enterprises must be given an important place. In a later chapter¹, statistics are quoted to show the extent to which the taxation of corporate enterprises has increased in the post-war period. Such taxation has been a powerful incentive to the financing of industry by debt rather than risk-bearing equities.

Since such fiscal reasons reinforced those arising from the economic and political instability of the post-war decade and

¹ Chapter IX.

from the effort to maintain existing price-levels and existing industrial organisation, industry was in fact financed in increasing degree by the incurring of debt rather than by the issue of shares direct to the investing public. The natural result of this method of financing business enterprise is to make profits more sensitive and variable. If prices increase or production costs decrease, a boom in industrial shares is easily begun. If, on the contrary, depression sets in, profits are quickly eliminated by the burden of fixed interest charges. From the banking point of view, the great danger is that such fluctuations, particularly in a downward direction, impair the security and liquidity of bank assets and thereby endanger currency stability. Banks which have large industrial commitments find their assets frozen and are forced to exercise more direct control over business enterprises.

A further consequence of the industrial activities of the banks in many countries was a strong impetus to consolidation. The consolidation and reorganisation of German banks in the depression is an example. The inevitable result of such a tendency is that the whole structure of expanded credit in a weak debtor country tends to become concentrated in a small group of banks or even in a single institution. When strain becomes intolerable, it seems impossible to allow that institution or any of its subsidiaries to collapse, and therefore steps are taken by the Central Bank and the Government concerned to support them. Liquidation is postponed, but at the cost of tying up both the currency mechanism and the budgetary system.

(v) THE STRUGGLE FOR LIQUIDITY.

Money market conditions after the depression fall into three fairly well-defined periods, the main features of which have already been summarised in Chapter II. The first period, from the break of the New York stock market in October 1929 to about the middle of 1930, was characterised on the whole by a measure of relief from the strain upon banking resources which had been caused by the stock exchange boom. During the course of 1929, the profits of speculation had drawn to New York an increasing amount of short-term credit. Rediscount rates were raised in New York and market rates were high. Short-term balances were profitably employed therefore for some months in the later stages of the boom in supporting speculation by means of brokers' loans. When the speculation collapsed, the tension in other money markets was relieved, discount rates were lowered, international lending was resumed for a few months in 1930, and

there was a period of relative monetary ease in which no very significant alterations in monetary policy were necessary.

In the latter part of 1930, however, it became apparent that the forces making for falling prices and difficulties in the balancing of international accounts were increasing in strength. The repatriation of French short-term balances continued steadily and was reinforced by a growing flight of short-term capital from many centres, not only to France, but to other continental money markets which appeared to be relatively secure. Many of the borrowing countries were in serious difficulties with their balances of payments.

Throughout the winter and spring of 1930-31, therefore, there was a growing credit stringency in the borrowing countries — including the United Kingdom, which was a considerable debtor on short term with long-term assets that were increasingly difficult to realise. At the same time, there was a rapid accumulation of short-term funds in the creditor money markets, despite low discount rates and similar measures intended to redistribute both credit and gold reserves. The Bank of International Settlements was preoccupied with this problem, but the price disequilibria and the existing feeling of political and economic insecurity were such that the situation went from bad to worse.

The third period, which can be described only as one of financial panic, was ushered in by the revelation of the embarrassed position into which the Austrian Credit-Anstalt had drifted. Its position became generally known in May 1931, and, from that time onward, the financial situation grew worse with alarming rapidity. The flight of short-term capital in the middle of the year from the London money market, which was deeply implicated in central Europe and had troubles of its own, ended in the United Kingdom abandoning the gold standard on September 21st. From that time till the present, the changes in banking policy which had been slowly gathering way, were accelerated into a competitive struggle for liquidity in the course of which the banking systems of those countries which endeavoured to remain on the gold standard have been forced either into progressive deflation or into virtual paralysis.

The course of events may be traced in the statistics showing the concentration of gold reserves which have already been set out in Chapter VI; and in those of note issues, exchange rates, and commercial bank deposits, all of which are regularly published in the League's *Monthly Bulletin of Statistics*.

The statistics of commercial bank deposits are set out in the table below for a number of important countries.

Commercial Bank Deposits, 1929-1932¹
(000,000's.)

Country	Cur- rency	End of Year			Average of First Quarter	
		1929	1930	1931	1931	1932
South Africa	£	61 ²	61 ²	61 ²	63	53
Germany. . .	RM	12,113 ³	11,207 ³	8,057 ³	10,486 ⁴	7,857 ⁴
Argentina . .	Peso	3,828	3,851	3,427	3,798	...
Australia . .	£	277 ⁵	263 ⁵	268 ⁵	263	289
Canada . . .	\$	2,163	2,068	1,927	1,996	1,884
United States . . .	\$	32,182	32,314	27,438	32,028	25,913
France. . . .	Fr.	34,065	36,681	38,245	37,149	37,404
Italy	Lira	16,911	17,965	16,335	17,786 ⁶	...
Japan	Yen	10,127	9,628	9,081	9,550	8,726
New Zealand United Kingdom.	£	55	52	52	54	54
Sweden . . .	Kr.	1,773	1,838	1,714	1,746	1,631
		3,481	3,631	3,554	3,713	3,656

It is evident that, in the first two years of the depression, there was little reduction of bank deposits in most countries. In many countries, indeed, there were substantial increases, measuring the extent to which industry was supported by the banks in the first shock of the crisis. The chief exception was in Germany, where deposits fell considerably, even in 1930.

In 1931, reductions were more general, but by no means universal. The heaviest fall among the countries shown in the preceding table was in Germany, which experienced a flight of capital and severe credit contraction.

There was also a sharp reduction in the United States, but in France there was an increase.

Before proceeding further to an analysis of these different movements, it is, however, necessary to point out that the statistics of total deposits conceal the important divergence between

¹ Compiled from *Monthly Bulletin of Statistics*.

² Average of year.

³ End of November.

⁴ Average of February and March, no returns available for January.

⁵ Average of last quarter.

⁶ At end of February.

the movements of time and demand deposits commented on in the previous section. This is clearly brought about in the following table :

*Percentage Change in Demand and Time Deposits,
1929-1931.¹*

Country	Demand deposits	Time deposits
South Africa	— 10	+ 17
Argentine	— 19	— 5
Australia	— 10	+ 5
Canada	— 22	— 5
United States	— 16	— 12
France	+ 12	+ 14
Japan	— 18	— 7
New Zealand	— 29	+ 14
United Kingdom	— 8	+ 2
Sweden	— 7	+ 6

Of the countries for which statistics are readily available, France is the only one in which current accounts and short-term deposits have increased. There has been a concentration of short-term money in the countries of which France is the type. There are great variations in the movements of long-term accounts, but the general tendency has obviously been for a severe restriction of current credit to develop in the great majority of countries, the resources withdrawn from business activity being placed either on long-term account or on short-term account in money markets, such as Paris, which are financially strong.

Such a movement is quite sufficient to explain the drastic deflation of the price level, in spite of the continuance of the total amount of deposits at a very high level. The statistics available for the early months of 1932 show that this process of deflation has continued strongly in most countries and especially in the United States and the United Kingdom, but shows some signs of coming to an end.

¹ *Monthly Bulletin of Statistics.*

Percentage Change in Demand and Time Deposits between the First Quarter of 1931 and the First Quarter of 1932.

Country	Demand deposits.	Time deposits
South Africa	— 16	— 17
Australia	+ 11	+ 9
Canada	— 10	— 4
United States	— 19	— 19
France	+ 2	— 25
Japan	— 13	— 7
New Zealand	— 6	+ 6
United Kingdom	— 12	nil
Sweden	— 8	+ 2

The strong deflationary movement evident in this table is only partly due to the repatriation of French and other continental short-term balances, a movement which slowed up in early 1932 and was practically completed by the middle of the year. It was caused largely by the effects of the financial panic which drove the banks, particularly of the United States of America, into a competitive struggle for liquidity. This struggle which reached its height in the spring of 1932, was accompanied by forced liquidation of security holdings which drove security prices down to very low levels and caused a very large and alarming number of bankruptcies. In the United States, the liquidity crisis bore all the marks of a panic, and recent banking legislation and practice were mainly designed to combat this situation. The Gold Delegation, in a general reference to the problem of credit contraction, stated its opinion that "where credit contraction for one reason or another has been carried to extremes, it is proper, and, indeed, imperative for the Central Bank to take such action as may be within its power to check excessive contraction, and, in some cases, to take the initiative in encouraging a freer use of credit".

The statistics used above must be read in the light of the currency depreciation that took place in many countries, especially after the United Kingdom abandoned the gold standard in September 1931. An apparent increase in deposits — for example, as shown for Australia in the last table — must be corrected for the heavy depreciation of the currency which, in Australia, was 25 per cent below sterling in March 1932, while sterling was 25 per cent below gold parity, so that the Australian currency was approximately 44 per cent below gold parity. The contraction of demand deposits in other countries with depreciated currency

bears witness to the very great deflation that took place in the course of 1931 and 1932.

The hoarding of credit, either in long-term deposits or in short-term foreign balances, has been paralleled by a hoarding of banknotes in certain gold-standard countries and of gold itself¹. An increased issue of paper currency may be due either to inflation denoting a lowering of the gold value of the currency, to an increased demand for circulation, or to a demand for hoarding. It might reasonably have been expected that the decline of industry and trade and the much lower levels of prices in the depression would have reduced the demand for banknotes, and this has actually been the case in most countries.² There are many examples, however, of increased issues called forth by hoarding—notably in France, Netherlands, Belgium, Switzerland and the United States of America—and other cases where increased or sustained issues are correlated with inflation. In the latter cases, the inflation is sometimes accompanied by a depreciation of the external value of the currency; in others, the currency is maintained nominally at par, although a “black market” exists where the depreciation is recognised. The statistics of notes issued during the depression are reproduced in an appendix to this volume.

During the course of the depression, currency depreciation occurred in many countries. The extent and development of this depreciation is best shown by the accompanying diagrams, the first of which shows the course of exchange in the United Kingdom and those countries which followed the United Kingdom off the gold standard. For comparison, Canada is included in this group. The second group consists of some Latin-American countries, and the third of four countries, Greece, Spain, China and Japan, whose currencies have depreciated for different reasons.

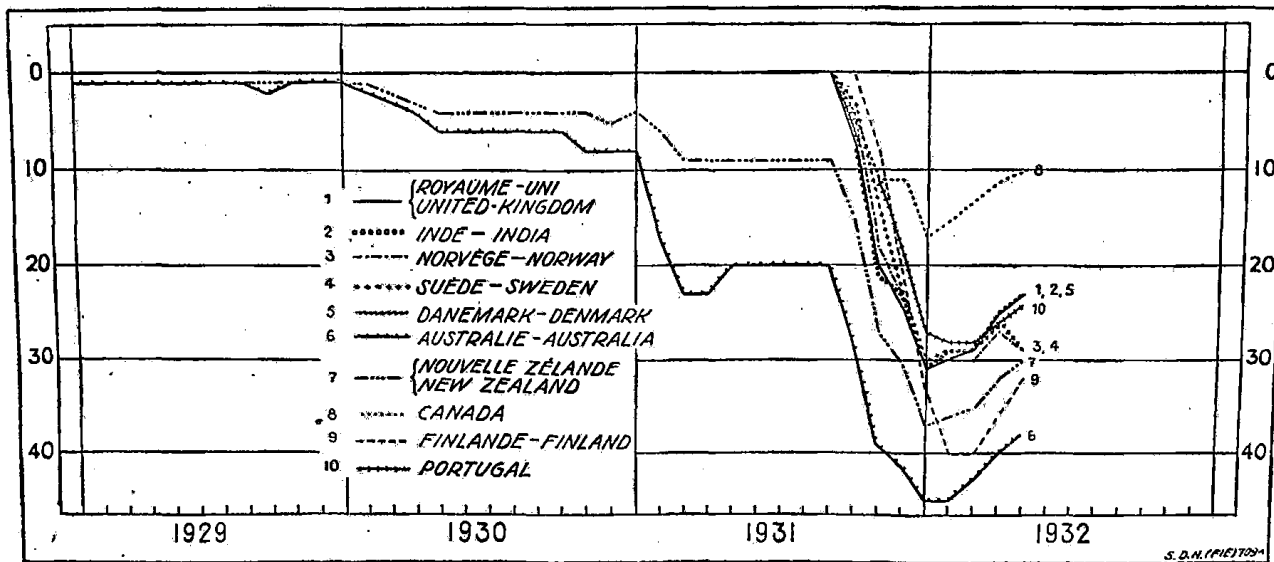
There is, on the whole, a remarkable similarity of movement in the exchanges of the so-called “sterling group”, showing that the currencies of several countries have been managed mainly with reference to their relation to sterling. The tendency for this group to rise again, after the low point touched in December 1931, is noticeable.

With the disruption of the international monetary mechanism by reason of the widespread abandonment of the gold standard, banking policy was thrown into confusion in the latter part of 1931. A new and disturbing element—fluctuating exchange rates—was added to those which had already made the conduct

¹ Cf. the estimate made by the Gold Delegation in its final report, paragraph 125 (\$400,000,000 in the last six months of 1931).

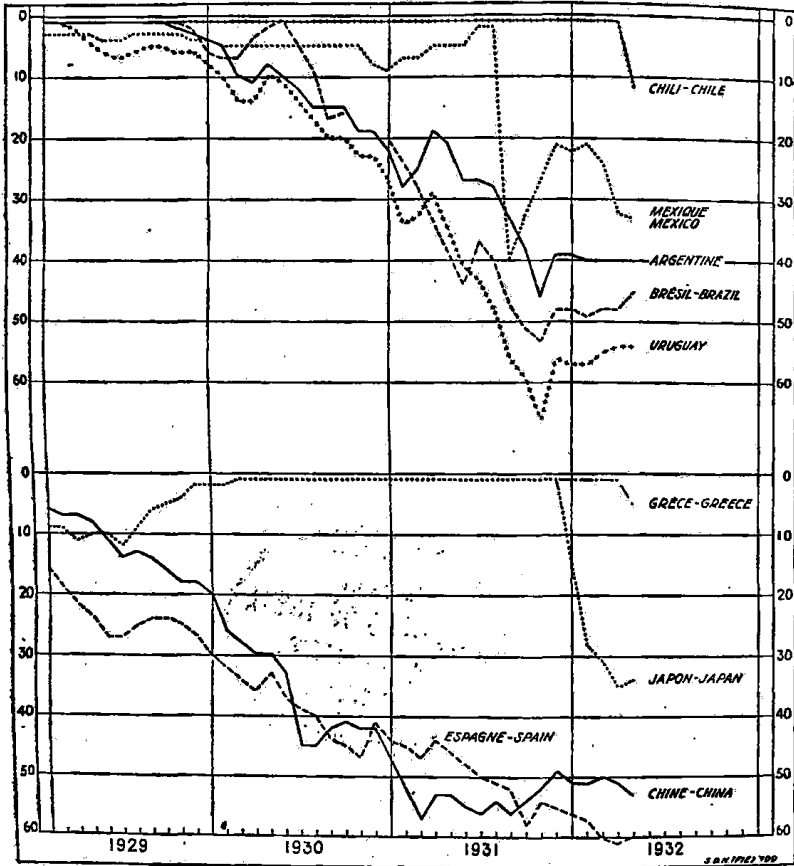
² See *Monthly Bulletin of Statistics*.

The Course of Exchange on New York, 1929-1932.
 (Discount per cent of various national currencies in terms of gold parity as expressed in U. S. Dollars).



The Course of Exchange on New York, 1929-1932.

(Discount per cent of various national currencies in terms of gold parity as expressed in U. S. dollars).



of banking extremely difficult. The Gold Delegation's summary of the international position in June 1932 was that "with only some six countries maintaining an unrestricted gold standard, the functioning of that standard as an international monetary mechanism has been greatly restricted. Side by side with it, there now exists a variety of other currencies whose exchange relations with the gold countries and with each other are no longer kept in equilibrium by their common relationship to gold, but must be governed by other means. Some of these currencies are on an independent basis of inconvertible paper, a large group of them being maintained at parity with sterling; others are maintained at nominal gold parity by the control of foreign payments and foreign trade."¹

In face of this situation, it becomes more convenient to discuss the most recent developments of banking policy in a later chapter. This is unfortunately a logical sequence to follow, since the depression which began largely as a result of increasing credit stringency in the agricultural borrowing countries has progressed through the stages of an acute financial crisis to a point where the immediate problem confronting the world is to stave off a further deterioration likely to result in a collapse of the banking and credit mechanism in many important countries.

¹ *Report of the Gold Delegation of the Financial Committee, paragraph 74.*

Chapter VIII.

WAGES, UNEMPLOYMENT AND LABOUR CONDITIONS.

(i) A RISING STANDARD OF LIVING.

There can be no reasonable doubt that, in the first post-war decade, the forces working towards higher standards of living were very strong in practically every country of the world. In the first place, there was a great acceleration of productive activity, particularly after 1925. The consequences of such an acceleration were somewhat confused by the fact that there were inevitably considerable transformations of industry in most countries. Many older-established industries, particularly those catering for the simpler basic demands such as food and clothing, either languished or progressed at a much slower pace than the industries created to meet newer demands, particularly for the employment of leisure. There was a considerable upward shift in demand, away from the basic necessities of life to the more elaborate requirements of individual taste. Large and important sections of industrial life — the coal industry, cotton and woollen manufactures, and agriculture in most countries — did not share fully in the general expansion of industry. Moreover, technical progress was one of the main causes of increasing production, and the primary labouring processes, therefore, were relatively less used. In such a period of rapid economic change, there are always eddies and backwaters of relative stagnation; but the main current was obviously in the direction of satisfying a wider range of secondary demands. Production was outrunning the simpler wants.

In the wealthier countries, especially, there was a notable democratic extension of purchasing power, by reason of higher wages, the lower costs of mass-production by rationalised methods, and new devices of merchandising, such as the instalment system. The rapid development of the cheap motor-car is a striking example, to which may be added that of other typically mechanical productions, such as wireless sets and gramophones. It has already been argued that the investment boom of the years 1925 to 1929 was primarily directed towards the production

of such articles of durable consumption.¹ It is, indeed, clear that such investment, based upon the expansion of cheap credit, finally overran the actual savings of the community and was one of the chief causes of the crisis and subsequent depression.

This fact — over-investment in the industries producing goods of durable consumption — is quite compatible with, and is indeed the complement of, the failure of purchasing power to keep pace with production in the later stages of the boom. The increasing volume of production in general and the marked tendency for it to be concentrated in these newer industries were based firmly enough upon demands created in the first instance by increased efficiency of production; but, aided by credit expansion, these demands stimulated investment to a point beyond the purchasing-power capacity even of the wealthiest countries.

While these facts were perhaps not so obvious in the countries which started from lower levels of purchasing power, and particularly in those which were impoverished by the war and the disturbances to economic organisation generated by the war, there was almost universally, in the boom years 1925 to 1929, a considerable advance in the standard of living of the masses of the people.

Apart from the fact of increasing productivity, account must be taken of the strong influence of organised labour. There was not only a greater national income to divide, but wage-labour was able to gain a relatively greater share.² During the war period and in the war settlement, the claims of the trade unions were forcibly presented and, despite some loss of bargaining position in the depressions of 1920-21 and 1929-1932, their power, both in the economic and in the political sphere, remains strong. Labour organisation, however, is most firmly entrenched in the more highly organised manufacturing industries, and there are large sections of the economic community which have not succeeded in building up a parallel defensive organisation. This is true, for example, of a great part of the working farm population, as well as of the salaried, professional and middle classes. In the periods of drastic economic readjustment, such as those caused by the violent post-war currency inflation in many European countries, the organised workers were able to maintain their status in the community much more successfully than many of these other groups.

Statistical material concerning wage-movements is not wholly satisfactory. In many countries there exist indices of wage rates or of earnings, hourly, daily or weekly; but there are few

¹ See Chapter II, section (f).

² Cf. W. H. Beveridge, *Unemployment: A Problem of Industry*, London: Longmans, Green and Co., 1930, Chapter XVI.

measurements of annual earnings, and almost none of earnings over longer periods of working life. It is, moreover, extremely difficult to make accurate comparisons either between the earnings of wage-labourers as a group and other groups in the community, or between real earnings in similar industries in different countries. There is some evidence that recorded wage rates tend to underestimate the remuneration of labour, since they do not allow for increases in piecework earnings, or for the regrading of labour which has tended to increase the proportion of workers in the higher-paid groups.¹ On the other hand, it is obvious that considerable allowance must be made, in any calculation of total earnings, for unemployment and irregularity of employment.

The evidence of such indices as are available points to a general and fairly substantial increase of real wages in the post-war period. The following table, summarised from *The International Labour Office Year-Book, 1931*,² gives convincing evidence of this increase. The statistics are not comparable as between countries, nor do they purport to measure the exact increase of earnings; but they do show the general direction of the movements.³

Index Numbers of Real Wages.

Country	Index	1914	1924	1929	1930	1931
South Africa .	Weekly rates — Men . . .	100	101	104	106	107
Australia . . .	Weekly rates — Full-time adult males	100	116	114	122	.
United States.	Weekly earnings — Men and women	100	129	142	135	.
Germany. . .	Hourly rates — Skilled men and women	100	.	110	116	.
	Skilled men . . . . .	.	.	.	114	117
United Kingdom. .	Weekly rates — Men and women	100	100	109	112	117
Sweden . . .	Daily earnings — Men and women	100	121	138	146	.
Czechoslovakia	Weekly rates — Men and women	100	114	119	121	127

¹ Cf. G. D. H. Cole, *British Trade and Industry: Past and Future*, London: Macmillan, 1932, page 303.

² For recent figures, see *International Labour Review*, February and May 1932.

³ See also *The Course and Phases of the World Economic Depression*, pages 83-87 and 172-173.

Apart from direct increases of earnings, however, there has been an increasing tendency towards the augmentation of "real income" by the provision of public services. In the nature of the case, these services cannot be subject to exact statistical presentation. They range from the efforts of State and municipal enterprise in the field of commercial and trading undertakings and public utilities to direct subsidies of various categories of the population. Many of them have social as well as economic justification, as in the case of the provision of pure-water supplies and drainage systems. The social factor is predominant in others, such as education and many municipal amenities; but there exist also a large number of trading enterprises, especially in the field of transport, which have economic justification but often involve a net cost to the taxpayer.

The general drift of the public utility and social services is almost inevitably in the direction of redistributing income in favour of the poorer classes. Such services must aim at universality, and they tend to be used more by those who cannot afford alternatives. A great part of the "real income" of everybody is now furnished by community services; but this part is naturally greater in the case of the small incomes. Taxation, on the other hand, is progressive on the larger incomes. The provision of an increasing range of public services, therefore, provides a larger real income for a great number of the lower-paid members of a community partly at the expense of the wealthier.

This fact is clearest in the case of such direct payments as pensions, family allowances, and benefits of various kinds, of which the outstanding example in recent years has been for unemployment. Subsidies of unemployment insurance schemes, the provision of relief employment out of public funds or the direct payment of relief to unoccupied workers have been greatly extended in almost every country in the post-war years, and particularly since the onset of the depression.

The effect of such payments raises the standard of living of those concerned, not only by the prevention of destitution through the assurance of at least a minimum subsistence, but also by reducing the insecurity of livelihood which in former depressions has weighed heavily upon the working people. The "right to live", if not the "right to work", has been much more firmly established. Moreover, the existence of such measures materially strengthens the resistance offered by organised labour to wage reductions and indirectly assists the maintenance of existing standards of remuneration. The widespread acceptance of the notion of "standards of living", and the associated conception of a "minimum standard" which society

should in some way guarantee to every normal individual, is one of the most remarkable social developments of recent years. Trade unionists and social reformers have fought for this conception for many decades ; but its acceptance has been much more general in the post-war period. The contractual idea which it embodies is of profound importance and marks a distinct departure from theories of individual enterprise and free competition. It establishes, in economic organisation, a new social right comparable in many ways with property rights.

The legislative movement towards improvement of working conditions ought not to be ignored in this connection. The increased political influence of trade-union organisation in many countries since the war has given a strong impetus to this movement. A survey of national legislation in such matters as hours of work, weekly rest periods, night work, holidays, industrial physiology, pathology and hygiene, occupational diseases, industrial accidents, women's work, the protection of children and young persons, and factory inspection discloses great variations from one country to another ; but the general impression gained is one of rather rapid progress.¹

The pace of national legislation has undoubtedly been hastened by the creation of the International Labour Organisation under Part XIII of the Treaty of Versailles. The mere existence of regular international assemblies concentrated on the discussion of these and related problems, and supported by a considerable body of committees as well as a permanent international secretariat, focuses attention upon comparative labour conditions. It provides a means, also, for an approach to international action on many problems where the fear of industrial competition has hitherto checked national legislation. By February 1st, 1932, a total of 452 ratifications of the various conventions recommended by successive conferences had been received, while 55 more had been authorised and a further 121 recommended.

The general assumption upon which the whole of this legislation, national and international, proceeds, apart from considerations of justice and humanity, is that its long-run effect is to improve the welfare, and therefore the efficiency, of the workers. It is argued that the experience of almost a century of factory legislation has proved that, in the long run, regulation and improvement of working conditions does not add to the costs of production, but, on the contrary, lowers them. The same general argument underlies much of the activity in social welfare

¹ Cf. International Labour Office, *Annual Review, 1930*, and *The I.L.O. Year-Book, 1931*.

legislation to which reference has been made above, and is powerful also, in various forms, in all efforts to raise wage-levels and standards of living. It is clear that this conception, based largely on past experience, has gained much more general acceptance since the war.

The "policy of high wages", indeed, has not depended for support wholly upon arguments derived from humanitarian or social grounds, or from considerations of efficiency. A strong body of opinion, particularly in the United States, among employers as well as among employees, has grown to favour liberal wage policies, combined with improved management and technical progress leading to lower prices, as a means of maintaining "purchasing power". This general view has too many facets for any brief summary to be adequate. It is closely connected with the desire to extend markets downward into lower ranges of income, in order that the increased demands thus liberated may make possible the economies of standardised mass-production. This is not the place to examine the validity or the limits of such a doctrine. Its existence should be recognised, however, as one of the forces making for higher wage rates, shorter hours and improved working conditions.

Any attempt to estimate the proportion of national income in various countries which is received directly by workers in the form of wages encounters, not only a paucity of statistical information, but very considerable difficulties of definition. The proportion of wage-earners in the working community, as compared with those of independent small masters or salaried persons, is by no means constant, but varies considerably between different countries and in the same country at different times. At a certain stage of industrial development, the independent craftsman tends to be crowded out by the competition of larger units of production employing wage-labour; but a stage is reached later at which the rationalisation of industrial processes tends to reduce the wage-labour required, so that the displaced workers become salaried employees or endeavour to find new and often independent occupations. The much greater increase in salaries than in wages during the post-war decade in the United States is partly due to this development, which on the whole represents an economic gain.

With this qualification in mind, it is permissible to conclude from the summary table below that, in the countries where statistics are available, wage-payments during the first decade after the war at least maintained their relative share of the national income. It is probable, indeed, that the proportion of national income directly paid to the workers in the form of wages and salaries increased. When the indirect provision of

“ real income ” noted above is considered also, it becomes clear that the standard of living has risen substantially. ¹

Percentage of National Income paid as Wages, Wages and Salaries, or Earned Incomes. ²

(I, Wages ; II, Wages and Salaries ; III, Earned Incomes.)

Year	Australia	Belgium	France	Germany	United States		United Kingdom	
	III	I	II	II	I	II	I	III
1911	56.2 ³						43	75.5
1913		34	43.6	45	36.4	52.7		
1924	54.4	38	46.4		37.7	57.7	43-45	78.0
1925	62.2		44.5	56	37.6	57.2		
1926			43.6	56	38.1	58.2		
1927		42	44.1	55	37.3	58.2		
1928			44.4	57	36.0	57.2		
1929	57.0			57				
1930		41		58				

The bearing of this conclusion upon the development of the crisis of 1929 and the subsequent depression has two aspects. Not only the actual levels of wages, but their flexibility, prove to be important in periods of fluctuating prices. As subsequent sections of this chapter will show, levels of wages are not only relatively higher than they were, but they are more resistant to reductions in a time of falling prices. So large a part is played now in the determination of wage-levels by collective agreements,

¹ The table above is not inconsistent with the fact that, in the boom period, the increases in production were much greater than the recorded changes in wage rates. Information is fragmentary, but it may be noted that this discrepancy was greatest in the countries of most pronounced credit expansion. Between 1924 and 1929, production in the United States increased by 25 per cent, whereas wage rates increased only 8 per cent. Steadier employment and higher earnings reduced this gap, but the proportion of national income paid in wages fell appreciably. In Sweden, production increased by 30 per cent and wage rates by 13 per cent, while the proportion of earnings also fell.

² Sources :

- Australia : Sutcliffe “ The Australian National Dividend ”, *Economic Record*, 1926, and Copland and Shann, *The Crisis in Australian Finance*, Sydney, Angus Robertson, 1931.
- Belgium : *Bulletin de la Banque Nationale*, 1930, page 377.
- France : *Bulletin de la Statistique Générale de la France*, 1931, page 557.
- Germany : *Statistisches Jahrbuch*, 1931, page 352.
- United States : King, *The National Income*, page 80; New York: National Bureau of Economic Research, 1930.
- United Kingdom : Bowley and Stamp, *The National Income*, page 50; Oxford: Clarendon Press, 1927.

³ 1907.

and in some cases by legislation, that not even severe and prolonged unemployment brings about the reductions that used to be relied upon as one measure of adjustment in crises.

This rigidity at a higher level is, of course, paralleled by other developments of the economic structure, particularly by the greatly increased volume of debt and high rates of interest. The distributive struggle which is a necessary part of any economic order based upon free enterprise has taken a new turn with the development of the contractual idea in wage payments as well as in debt commitments. It has been argued earlier¹ that the greater proportions of the national income claimed, on the one side, for debt service and, on the other, for wage payments, both of which categories are regarded as fixed and invariable, have concentrated the pressure of deflation, after the breakdown of the credit expansion in 1929, upon the more variable shares in national income, and particularly upon the profits of business enterprise, with the result that the mainspring of economic effort under the present system has been weakened. Restoration of the profits of enterprise, in default of a rise in prices, necessitates a reduction either of the debt claims or of the standard of living of the workers, perhaps of both. In the crisis as it stands in the spring of 1932, schemes and projects of a more permanent character, such as the various proposals, on the one hand, for a reversion to a freer, or, on the other, progress towards a more completely planned, economic organisation, must necessarily wait upon a measure of recovery from depression. Economic activity must be revived before it can be reorganised, and any restorative measures involve some sacrifice of claims at present rigidly maintained in face of shrunken national incomes.

The various methods which have been proposed as ways of escape from this dilemma fall into two main classes — the restrictive or deflationary group, which tends to concentrate upon readjustment by reductions of present claims upon production, and particularly by wage reductions; and the expansionist or inflationary group, which plans monetary or other measures designed to restore a higher level of prices, without cutting down the nominal value of present claims. While there are an almost infinite variety of plans proposed, and the broad distinction drawn above ignores many essential complications of an extremely difficult problem, it remains broadly true that the chief division of opinion lies between those who advocate measures of deflation which place a large proportion of the cost of readjustment upon what they regard as untenable standards of

¹ Chapter I, section (vii).

living, and those whose advocacy of inflationary measures is based largely upon the belief that higher levels of prices would reduce the real burden of debt services.

(ii) WAGES IN THE DEPRESSION PERIOD.

The advent of severe economic depression characterised by an extremely sharp and long-continued fall of commodity prices not only raised into clear relief the extent to which the new conception of the standard of living had gained acceptance, but also challenged its economic validity. It was not, indeed, until a comparatively late stage of the depression that attacks upon the standard gathered force. In 1930, the unanimity with which it was agreed that the maintenance of existing standards was both right and expedient was quite remarkable. The persistence and intractability of the depression gradually undermined this attitude, and by the beginning of 1932 strong deflationary policies were in operation in many countries.

The whole problem was complicated by the fact that, in the preceding period of credit expansion, particularly in the years 1925 to 1929, the maintenance of cheap rates of short-term credit together with high long-term rates of interest had over-extended consumption, particularly of certain new manufactured commodities. Attention has been paid, in previous chapters of this *Survey*, to the disturbing effects of this credit expansion in many varied aspects of economic organisation — the misdirection of capital to over-developed consumption industries and to unproductive "distress" borrowing, largely for consumption purposes; the maintenance of high agricultural price-levels on the basis of valorisation schemes; the promotion of security speculation. The most important effects of these disturbances, it has been argued, were the maintenance for a time of consumption at a very high level and the consequent pressure that was gradually exerted upon the profits of business enterprise. In the inflation period, therefore, some part of the gain in wage rates and the rapid increase of "real income" by the provision of social services — achieved, as it was, contemporaneously with a heavy accumulation of debt obligations — was really made at the expense of capital consumption.

In other words, the post-war advance in the standard of living (and in capital investment of various types) was compounded of two elements — the first a genuine increase in production caused by rapid technical progress and the restoration of world trade; the other a fortuitous addition by credit expansion which created the possibility of still more extended consumption, in anticipation of which an investment boom reached large

proportions. During the boom, serious maladjustments inevitably took place. In its final stages, investment in the new industries producing goods for "durable" consumption outran the purchasing power of their consumers, because this was dependent upon the earning power of industry in general, and the forced development of the new consumption industries drained capital resources from the remainder of the industrial organisation. It is this fact which limits the prospect, by further credit expansion, of righting the balance by putting more purchasing power in the hands of consumers. Each fresh dose of credit intended to increase purchasing power in fact aggravates the maladjustment in the long run, unless at the same time there is a considerable liquidation of existing claims on industry.

When the boom burst in October 1929, the economic organisation of the world had been saddled with heavier monetary claims upon its produce — with much greater obligations of debt on the one hand, and with higher standards of living and wage payments which were embedded in social approval on the other. Expansion of credit had stimulated a forced and uneven economic development in the course of which capital had been wasted, partly by over-extended consumption, but latterly, also, by investment which was misdirected in anticipation of still further extensions of consuming power. If an example may be over-simplified, the world was tempted by cheap credit, first into buying more motor-cars than its resources would in reality permit (due regard being had to other wants), and then into providing equipment for making still more motor-cars, on the assumption that demand would continue to increase at the artificially stimulated rate. It attempted, by the self-deception of book-keeping, to arrive immediately at the legitimate goal of higher living standards which it had in fact been steadily approaching by the slower but substantial progress of organised real effort. In the result, not only the inflated standards of the boom, but also the hardly-won gains of genuine technical progress, are in danger of being lost.

The processes by which the diversion, in the pre-depression period, of capital resources into channels which were partly wasteful caused a severe fall in commodity prices have already been discussed.¹ When the price-level began to fall, a situation of deadlock was created, since much heavier debt obligations and improved standards of living were incompatible with a greatly shrunken nominal income. The distributive conflict between the remuneration of capital and that of labour was immensely aggravated. Reduction of the claims upon industry became

¹ See Chapter II, section (i).

inevitable, since both the nominal and the real value of total production shrank. The shrinkage in nominal value because of a falling price-level was not the result of a simple and uniform scaling down of prices, but a very rough and harsh dragging down of those prices which had least resistance. So many maladjustments are created in this process that there is inevitably a shrinkage of production, thus reducing the real as well as the nominal value of the total product. The extent of this paralysis of productive effort has already been disclosed.¹ It is, unfortunately, a cumulative process until such time as the claims to shares in the total produce of industry are reduced to levels which again make enterprise profitable, or until a fresh expansion credit is successfully launched.

In the present depression, the difficulties of any very real reduction of these claims have been greatly increased by the fact, previously examined,² that both capital claims and standards of living have proved to be more rigid and less capable of modification than in previous depressions. The capital market has been burdened with the enormous volume of claims originating in the waste of capital during the war, the spendthrift borrowing after the war and the misdirected and wasted investment in the period just before 1929. An unfortunately large proportion of the debts thus incurred has gone through the channels of public borrowing. The capital has been lost or used unproductively; but the claim is not written off and remains as a charge upon Governments, which they must transfer to industry in the form of heavy taxation. Another substantial proportion has gone through the channels of banking, and its loss or impairment has tied up the monetary systems of many countries, which thereupon have been supported by State guarantees. The liquidation of industrial capital, which is a normal consequence of depression, has not been able to rid industry of its excessive load, and cannot do so until taxation can be reduced and credit can be liberated by releasing the banks from their frozen advances. Moreover, the continuance of heavy taxation and insecure banking conditions continually increases the pressure upon what were sound productive investments. Existing plant lies idle, new capital cannot be tempted into industry and production diminishes.

In much the same way, the rigid maintenance of high nominal wage rates and of greatly increased social services and benefits has operated to prevent a scaling down of the labour claims upon the product of industry. Labour also is forced into idleness and the volume of unemployment constantly grows.

¹ See Chapter III.

² See Chapter I, section (vii).

At the commencement of the depression, there was almost worldwide failure to recognise the universality, complexity and gravity of the economic maladjustments that were destined to work themselves out relentlessly in a cumulative pressure of profit and income deflation. Mr. Lippmann has collected an impressive string of quotations from Government, business and economic authorities in the United States which sufficiently prove this point.¹ The keynote was struck by the President himself in his message to Congress in December 1929, when he announced that he had "instituted systematic, voluntary measures of co-operation . . . to make certain that the fundamental business of the country shall continue as usual, that wages and therefore consuming power shall not be reduced, that a special effort shall be made to expand construction work in order to assist in equalising other deficits in employment".

There was, in fact, not only in the United States but universally, a general attitude of maintaining existing claims to income. Wage rates were far from being the only claims which were sustained. A striking example may be cited in the tariff and farm relief legislation of the United States, where, in seeking to erect barricades against the first waves of depression, "certain theories were considered axiomatic by the President, by the majority in Congress and by dominant public opinion. They were that the existing levels of industrial profits, the existing volume of industrial employment and the existing rate of wages were normal and secure, and that, therefore, any economic activity, such as grain farming or the manufacture of textiles, which could not be operated on this plateau of prosperity, needed somehow to be raised to it."²

During the whole of 1930, in most countries for which records are available, nominal wage rates were maintained or increased, while the cost of living fell steadily, so that real wages of employed workers rose. The barricade of sustained purchasing power was, however, steadily undermined by increasing unemployment, by an increasingly rapid decline in commodity prices, and by the deeper and deeper embarrassment of one group of producers after another. At many sections of the barricade, indeed, such actions as the erection of higher tariff barriers, attempts to hold up agricultural prices and public works construction programmes, which either added to taxation or drained still more capital from industry, had the effect of damming up the forces of deflationary adjustment which, in consequence, first spread themselves over a wider area and then broke with irresistible

¹ Walter Lippmann, *The United States in World Affairs*; New York, Harper's, 1931, Chapters I and II.

² Lippmann, *op. cit.*, page 17.

force through the weaker parts of the structure. By the beginning of 1931, it was evident that hurriedly improvised conservatory measures could not cope with the situation ; but there had been little approach to any more radical solutions.

There were some notable exceptions to the general stabilisation of wage rates and standards of living even in 1930. Reductions began early in the more heavily indebted and weaker competitive countries and industries. As examples, there may be cited the steady downward drag in Japan under the pressure of monetary deflation from the beginning of 1930 ; the drastic reduction of the wages of plantation workers in Brazil after the collapse of the coffee valorisation scheme in 1930 ; and the fall of agricultural wages in both the United States and Canada in that year. These examples might be supplemented by others ; but their general significance is clear.

The daily rates of agricultural workers in the United States had stood at roughly 70 per cent above the pre-war level from 1925 to 1929 ; but in the last quarter of that year the index fell from 171 to 158. There it stayed during the first half of 1930 ; but after the collapse of the spring revival of that year, the pressure was steadily downwards. In the last quarter of 1931, the index stood at 110. This steady weakening of agricultural wages is in significant contrast with the maintenance of industrial wages which the President had secured by informal agreement at the outset of the depression. Even here, however, an increasing number of reductions in particular industries slowly lowered the average throughout the year. As late as July 1931, several spokesmen of the administration reasserted its policy of doing everything possible to avoid wage reductions ;¹ but the index, which had held almost steady at 238-239 through the first three quarters of 1930, dropped throughout 1931 till it stood at 215 in the last quarter of the year.

It is significant, moreover, that the weekly earnings showed a much more marked decline than the hourly rates, and a decline which began earlier. The statistics are reproduced as showing the extent to which short time was used in place of wage reduction.

Manufacturing Industries : General Index — Men and Women.

	1914	1929				1930				1931			
		III	VI	IX	XII	III	VI	IX	XII	III	VI	IX	XII
Hourly earnings .	100	236	238	238	238	238	239	238	234	230	227	225	215
Weekly earnings.	100	228	226	228	220	217	211	198	190	187	181	170	162

¹ *Industrial and Labour Information*, September 14th, 1931.

Towards the end of 1930, the whole wage situation in many countries began to be seriously affected by budgetary difficulties. When it became evident that the effort to maintain existing claims on industry without any means being discovered of stopping the fall in prices and production was beginning to undermine budgetary and therefore currency stability, these countries took drastic action. The first important country to embark on a considered and radical scheme of deflation was Italy. In November 1930, salaries and allowances were cut 12 per cent. At the same time, an extensive campaign of propaganda was aimed at a general wage reduction of approximately 10 per cent. It has been claimed that the corporative economic organisation of Italy enabled the Government more easily to break through the resistance of individual industries and interests in carrying out its programme of breaking the rigid structure of price and wage costs.

In the middle of 1931, many other countries followed this line of action, mainly for budgetary reasons. The outstanding example is Germany; but reference may be made also to the situation in Australia and New Zealand. In both these countries, the heavy fall of export prices had seriously lowered the national income, and the export industries in particular pressed for relief from heavy costs of production. The Commonwealth Arbitration Court opened a Basic Wage Enquiry on August 15th, 1930, and, despite intervention by the Commonwealth Government, on March 30th, 1931, the Court delivered final judgment which reduced the "real" basic wages of almost all workers under its jurisdiction by an average of 10 per cent. Some of the State tribunals followed suit; but in some States the existence of statutes prescribing basic wage rates prevented such reductions. In addition to the lowering of the basic rate, a continuous fall in the cost of living lowered nominal wages still further for those workers subject to the Commonwealth Arbitration Court. By October 1931, the total reduction approximated 23 per cent.¹ Under the Premier's plan, which was launched in May and June after a report by a committee of economists and treasury officials, Government expenditure was reduced, taxation increased, internal loans converted, interest rates reduced and relief given to mortgagors.²

The New Zealand Arbitration Court had reduced wages by 10 per cent on June 1st, 1931. In March of the following

¹ D. B. Copland, "Readjustment in Australia", *The Economic Journal*, December 1931, page 536.

² *Ibid.* See also F. A. Bland and R. C. Mills, "Financial Reconstruction", *Economic Record*, November 1931.

year, a scheme of retrenchment in some respects like that of Australia was introduced, together with a further wage and salary cut of 10 per cent.

In Germany there was some evidence of a downward pressure on wages, at least from the beginning of 1931. The Government's programme of retrenchment began with the 6 per cent cut in salaries in February, which initiated the practical measures announced in the Emergency Decree of December 1st, 1930. In Germany, 75 per cent of the total amount of wages and salaries was subject to determination by legislation or collective agreement. A very vigorous effort was necessary, therefore, to break through the maintenance of wage rates when budgetary equilibrium was threatened in the middle of 1931. Another Emergency Decree on June 5th reduced salaries and unemployment relief and the Hoover Moratorium gave temporary relief; but after the departure of Great Britain from the gold standard the strain was renewed. The Government's defence against devaluation of the currency took the form of the drastic and unprecedented measures contained in the fourth Emergency Decree of December 8th, 1931. A general wage reduction was part of the scheme, together with a lowering of cartel prices, public utility rates, house rent and interest rates. The general principle of wage reduction was to get back to the level of January 10th, 1927; provided the change did not involve more than a 10 per cent cut, the object being to get rid of the increases which occurred in the period of credit expansion 1925-9. As a total result of these various steps, the general index of wages in Germany has fallen from 107 in 1930 to 90 at the beginning of 1932.¹

In August 1931, budgetary difficulties had become evident in Great Britain also. Moreover, the pressure of circumstances had lowered purchasing power in British markets and in some cases reductions of wages had given an advantage to rival exporters. The export industries of most countries were feeling the strain of diminished purchasing power in the agricultural markets; but wage standards were for the most part tenaciously maintained despite a growing volume of unemployment. It was not till the latter part of 1931 that deflation in Italy, Germany and the United States and devaluation in Great Britain threatened to cause an international competition in lowering costs of production.

In Great Britain, trade-union organisation was strong enough to resist wage reductions in face of a serious decline in the export trades, increasing unemployment and a difficult budgetary

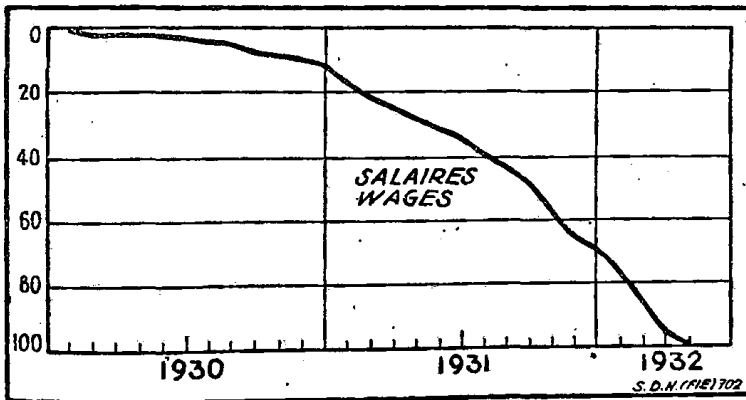
¹ *International Labour Review*, May 1932.

situation. In August 1931, the newly formed National Government carried through a reduction in Government expenditure, including that on salaries and on unemployment benefits, but industrial wage rates remained steady on the average. The pressure for reduction was eased when Great Britain abandoned gold in the following month.

The export advantage gained by Great Britain and those countries which followed her action in abandoning gold was partly met by drastic efforts to close domestic markets and so shelter the price and wage structure in the countries remaining on the gold standard. Many of them — Switzerland, Czechoslovakia, Poland and France, for example — still maintained their wage rates; but the United States, Italy and Germany began strong policies of wage reduction.

In the first half of 1932, the movement for wage reduction gathered force. A substantial proportion both of the industrial and of the agricultural countries had removed the immediate pressure on their wages and price systems by going off gold. The annual wage contracts made in Europe in the spring of 1932 felt the pressure and reductions were inevitable. Both in agricultural and in industrial industries, wages fell. Complete statistics are not available, but the summary table on page 83 and the diagram below will show the movement of wage rates in the depression period.

Cumulative Percentage of Total Reported Wage Reductions in the United States, by Months from January 1930 to April 1932.¹



¹ The National Industrial Conference Board : *Salary and Wage Policy in the Depression*. New York 1932.

*Index-Numbers of Money Wages*¹ — Average 1929 = 100.

Date	United States		Japan	Germany	Denmark	France
	Industries Hourly earnings	Agric- ulture (men) Daily rates	Industries Daily rates	Industries Hourly rates	Industries Hourly earnings	Mines Daily earnings
1929 III .	100	99	100		98	94
VI .	100	102	100		100	98
IX .	100	103	100		100	100
XII .	100	96	99	100	101	107
1930 III .	100	94	99	101	100	108
VI .	101	94	98	101	102	109
IX .	100	92	96	101	102	108
XII .	99	88	95	101	105	108
1931 III .	97	77	93	98	102	108
VI .	96	74	92	95	102	103
IX .	95	71	92	95	102	103
XII .	91	65	91	93	103	103
1932 III .						

Date	Italy	Poland	United Kingdom	Czecho- slovakia	Australia	New Zealand
	Agr., Mines, Ind., etc. Hourly earnings	Industries etc. Daily rates	Agr., Mines, Ind., etc. Weekly rates	Industries Hourly rates	Industries etc. Hourly rates	Agr., Mines, Ind., etc. Weekly rates
1929 III .	98	99	100	99	100	100
VI .	101	100	100	100	100	100
IX .	101	100	100	100	100	100
XII .	100	101		100	100	100
1930 III .	98	102	99	101	100	100
VI .	100	102	99	103	98	100
IX .	97	102	99	103	97	100
XII .	93	102	99	103	95	100
1931 III .	88	100	99	103	92	99
VI .	90	100	98	103	89	89
IX .	87	99	97	103	88	89
XII .	86	98	97	103		89
1932 III .	93		96			

¹ The index-numbers refer in general to the average for skilled and unskilled men and women, the index-numbers for France, Australia and New Zealand only to skilled and unskilled men.

The general impression gained from this table is very clear. Despite an increasing number of reductions in the latter part of the period covered, the resistance of wage rates to even the strong deflationary forces of such a severe depression has been most marked. The concept of a minimum guaranteed standard of living has evidently gained powerful acceptance in almost every country. As the liquidation of the crisis proceeds, the gains in the standards of wage payments which were based on the preceding credit expansion may be wiped out; but there is little sign of any tendency of the basic conception of a guaranteed standard being weakened.

(iii) THE EFFECTS OF THE DEPRESSION UPON SOCIAL POLICY.

Attention has already been drawn to the importance of social legislation in the post-war decade. Such legislation covers so wide a range and affects economic life in so many ways that its costs and the benefits derived from it are not capable of precise measurement. Social legislation has gained a great impetus in recent years. Precedents continually broaden, the provision of elementary education extends upwards to public support of higher education and downwards to measures of medical inspection and feeding of schoolchildren; the principle of pensions, once admitted, is applicable not only to old age but to widowhood and invalidity; insurance covers not only unemployment but accident risks. The general assumption of public interest in private welfare is, indeed, capable of application to an ever wider range of State action. Its development has already introduced a large element of "planning" into the social organisation of most modern communities.

The advent of a severe and prolonged depression, with its accompanying distress and individual hardships, inevitably creates a strain upon the various mechanisms built up to relieve poverty and promote welfare. The first effect of depression is clearly to throw a much heavier burden upon these mechanisms. The final section of this chapter draws attention to the magnitude of this burden in the case of unemployment insurance and relief. The rapid multiplication of claimants has in many cases destroyed any actuarial basis the various unemployment insurance schemes may have had and turned them rather into mechanisms for the redistribution of income. In the same way, economic depression inevitably increases the cost of all forms of social relief. More schoolchildren have to be fed by public action, reduced earnings and psychological strain increase the amount of sickness, and a far heavier expenditure is necessary for poor relief.

Moreover, in most cases statutory provision for these misfortunes is fixed in monetary terms, so that increased demands must for a time be met at fixed rates out of diminishing public income. As one result, rates of taxation, both national and local, are kept at a high level, if not actually increased. In this way, the costs of industry are adversely affected at a time when falling prices and reduced turnover have in any case diminished the profit-margin which is the chief incentive to enterprise. Borrowing for relief purposes, either by the State or by local governments, further adds to the difficulties of industry by drawing off capital from investment purposes to those of immediate consumption, while keeping the rates of interest high.

Any long-continued drain of this kind is bound to be reflected in budgetary difficulties, and these difficulties, which became acute in most States in the autumn of 1931, rendered it necessary to reconsider at least the rates and conditions of relief, and possibly the whole structure of the relief system. The continuance of depression, therefore, inevitably tests the economic soundness and the political basis of social policy.

Such facts as these lend special interest to the review of social policy in various countries undertaken by the International Labour Office and briefly summarised in the Report of the Director to the annual conference in April 1932.¹ In the preparation of this review, extensive use was made of special enquiries undertaken by correspondents of the International Labour Organisation in several countries. The general trend of the reports is clear. In Germany, "there has not been at any time any question of going back on the established principles of social insurance, and the endeavours made by the last ordinance to balance at a given level all the activities in the economic or labour departments of life in Germany has removed any impression that there could be any real attempt at social reaction". In Great Britain, "on the whole it cannot properly be said that there has been any social retrogression". In Poland, "working conditions in places where Government supervision and trade-union activity are exercised would not appear to have been changed to any appreciable degree". Much the same report is made of Roumania, Belgium, Czechoslovakia and France, where, indeed, "the depression period is rather noteworthy for the development of measures for the relief of the unemployed". Notable activity in social policy is reported also for Spain and for Brazil. In the United States also, the unprecedented severity of the depression has greatly increased the tendency towards

¹ Pages 20-25.

protective labour legislation, "clearly contrary to all tradition in the U. S. A. and to the individualistic spirit which inspires its policy". Various manifestations of this trend are noted — "some hundred Bills on old age pensions are at present before the Parliaments of thirty-nine States; five such Bills have been adopted; in sixteen States, Bills have been brought in for establishing public systems of unemployment insurance, and an original system of providing unemployment benefit has been introduced in the State of Wisconsin".

As a result of this survey of developments in many countries, the Director of the International Labour Office, after noting the adverse effects of the depression upon the life of working-class families, emphasises the general conclusion that "it is a fact of considerable historic importance that, in spite of the unprecedented depression, labour legislation has been almost unshaken in all countries, and that the principles of the protection of the workers and social insurance have been reaffirmed".

In qualification of this broad general conclusion, there may be noted some tendency for the pace of legislation to be slowed down, and also some definite readjustments of existing benefits in order to meet the pressure of lower prices and budgetary difficulties. Particulars of some early readjustments are given in the report cited. In Germany, "the general level of social insurance has been restored to the 1914 level, except as regards family assistance", and "several hundred thousand pensions have been stopped". In Great Britain, benefits have been somewhat reduced, contributions increased and tests imposed in the case of unemployment insurance, while subsidies — *e.g.*, to the national health insurance scheme — are reduced, as part of a general retrenchment policy. In Australia and New Zealand also, the social services have been retrenched — unemployment payments reduced, old-age and other pensions cut and, in New Zealand, family allowances abolished.

The general slowing-down of new legislation is not easy to estimate, since the political prospects of such measures are generally uncertain. The employers' group in the Governing Body of the International Labour Office, in October 1931, pressed for conservation and consolidation of results already achieved rather than the continued effort to press forward with new reforms which, in its judgment, "would involve additional costs for many countries, and so render more difficult the necessary adaptation to the new economic conditions". This plea, however, was overruled by the decision of the Governing Body to add further questions to its agenda for 1933.

While, therefore, the depression, particularly in its later stages of budgetary difficulty, has, in certain cases, somewhat

hampered the extension and even curtailed the scope of existing national and international legislation, the enormously significant fact has emerged that such legislation, guaranteeing a certain minimum of protection to wage-earners, has become an integral and apparently unshakable part of the social organisation of almost every country.

(iv) THE PROBLEM OF UNEMPLOYMENT.

Unemployment, in all its varied forms, is by no means a new problem. It is essentially a problem of organisation, present in some degree at all times in every economic system. The peasant farmer of China, whose holding is too small to keep him occupied much more than about a fourth of his time¹; the independent craft worker in Europe, whose receipts fall off in times of depression; the Lancashire mill-hand working short time; the labourer who works only two or three days a week in an American motor-car factory, all suffer, though in different ways, from the lack of remunerative work which, in other circumstances, throws men and women into total idleness. It is probable that, on the average, there is less employment, or more under-employment, in the simpler agricultural countries, and that this failure fully to utilise available human energy is one of the main causes of the low standard of living common in such countries. But, if the highly elaborated organisation of industrial countries both raises the standard of living and reduces the total volume of unemployment, the very elaboration of the organisation renders it more liable to break down. Moreover, such organisation tends to concentrate what unemployment there is upon the less fortunate workers and to render its cost to the individual very heavy. The necessity for public action to diminish unemployment and to relieve distress arising from it is therefore greater in the highly organised industrial countries than in the simpler agricultural communities. As industrial progress spreads, there is, on the average, less unemployment in the world as a whole; but it becomes more concentrated, more harsh in its incidence and more dangerous socially.

It is the periodic aggravation of such concentrated unemployment, leading as it does to social distress and deterioration, mainly in industrial countries, rather than the more diffused under-employment characteristic of agricultural organisation, which presents the most urgent social problem of the present day.

¹ J. L. Buck, *Chinese Farm Economy*: Chicago University Press, 1930, page 231.

It was well recognised, even before the war disturbed economic organisation so badly, that some measure of continuing or chronic unemployment was a characteristic feature of modern industrial life. This minimum of unemployment caused by technical progress, by changes in consumer's demand, by lack of mobility or economic quality in certain individuals, by poor organisation of the labour market, and similar causes, was increased from time to time by seasonal and cyclical fluctuations of economic activity. The extent of unemployment was greatest in winter, was aggravated in periods of economic depression, and apparently also was liable to be increased when there was a downward trend in the general level of prices.¹

Since the war, however, the volume of persistent or chronic unemployment has been very much greater and has become a serious social problem in many countries. In Great Britain, as late as 1919, the Government Actuary estimated an unemployment risk of 4.5 per cent of the insured workers,² and it was later suggested that the difference between this estimate and the much higher percentages registered in post-war years was "a rough indication of the specific addition to unemployment which must be attributed to the war."³ While the increase of unemployment during the post-war period is most obvious and more easily recognised in such countries as Great Britain and Germany, it is by no means confined to such countries. Complete statistics, particularly for the pre-war period, are not available for many countries; but there seems little doubt that the economic disorganisation of the post-war years, to which reference has already been made in various connections, increased very greatly the minimum of unemployment which may be regarded as chronic.

In the case of Great Britain, if 4.5 per cent was regarded as a normal percentage based on pre-war experience, the level of somewhat over 10 per cent which prevailed in the relatively good years 1927-1929 represented, at least in part, a substantial addition to (perhaps a doubling of) the minimum to be reckoned with. It was difficult to accept such a suggestion before the present depression; but the subsequent increase of the percentage in 1930-1932 to well over 20 per cent of the total insured workers is an indication that the cyclical aggravation of

¹ International Labour Office, Studies and Reports Series C.No.16: Geneva, 1931, pages 97-118.

² See discussion in Beveridge, *op. cit.*, Chapter XVI.

³ Henry Clay, *The Post-War Unemployment Problem*: London, Macmillan, 1929, page 29.

unemployment in that country now begins from a much greater minimum.

While this post-war increase in the irreducible minimum of chronic unemployment is perhaps not universal, since certain countries have enjoyed fairly long spells of prosperity and active business in the post-war decade, it is very widespread. Even in the prosperous countries, it is probable that short spells of unemployment for many workers were a greater problem than the statistics (or lack of statistics) indicate. The absence of provision for unemployment insurance or relief which is notable in many of the more fortunate countries is quite compatible with the existence of a fair volume of unemployment. Moreover, the stoppage of migration, especially in bad years, has minimised the apparent growth of unemployment in some countries. It is evident, for example, that, in both the United States and France, as well as in some of the British Dominions, the unemployment figures might have been considerably higher if restrictions had not been imposed on immigration.

A tabulation of such statistics as are available indicates that, even before the present depression set in, there was a large volume of unemployment in most countries. The reasons are not far to seek. The economic system works less smoothly than before the war. There is less confidence, and therefore less readiness to rely upon international co-operation in trade, investment, migration; important parts of the economic system, including wage payments in most countries, are more rigid; large-scale industrial methods have been making great strides — and therefore the difficulties of so organising industry as to occupy all the available workers are greatly increased. A rough calculation at the depth of the economic depression, in the spring of 1932, gives a total of 20-25 million workers unemployed in the world. This alarming total is very significant, but no less significant is the fact that, all through the prosperous years from 1925 to 1929, before the depression broke, there persisted a total of unemployment which may perhaps be guessed at 6-8 millions. That this is not an exaggerated guess may be judged from the incomplete statistics shown in the following table, which do not cover all countries, or all unemployment in most of the countries. The existence of chronic unemployment on this scale is evidence of economic maladjustment quite sufficient to explain the subsequent collapse in the depression years.

As the tabular statement shows very clearly, however, the onset of the depression has greatly increased the number of unemployed in practically every country. The latest statistics available at the moment of writing show that, in February and March 1932, unemployment was still increasing almost everywhere.

*National Unemployment Statistics at the End of Each Year
1925-1931.*¹

(000's omitted.)

Country	1925	1926	1927	1928	1929	1930	1931
Canada	12	9	12	13	24	37	40
Japan . . . . .	.	.	.	.	315	362	471
Germany	1,499	1,749	1,400	1,830	2,851	4,384	5,668
Austria	209	205	207	203	227	295	330
Belgium	27	18	35	28	29	118	164
Denmark	86	89	87	78	63	73	97
Danzig . . . . .	.	.	.	13	16	24	33
Estonia	3	4	4	8	6	6	9
Finland	2	2	2	3	9	9	17
France	1	17	27	8	11	23	177
Hungary	28	22	14	15	20	26	33
Irish Free State . . . . .	.	.	26	26	24	26	31
Italy	122	181	414	364	409	642	982
Latvia	5	5	6	14	8	10	22
Norway	26	31	29	24	22	27	35
Netherlands	45	36	45	38	49	81	147
Poland	311	190	165	126	185	300	312
Roumania . . . . .	.	.	14	72	7	36	49
Unit. Kingdom	1,243	1,431	1,194	1,334	1,344	2,500	2,671
Saar . . . . .	.	.	4	8	11	15	35
Sweden	46	48	51	50	54	83	110
Czechoslovakia . . . . .	.	.	46	39	53	240	486
Yugoslavia . . . . .	.	.	.	6	6	10	15
Australia	34	25	39	43	57	105	119
New Zealand	2	3	6	6	1	8	46
U.S.S.R.	951	1,289	1,352	1,616	1,310	240	.

Only in Australia and New Zealand had slight falls been registered in the three preceding months.² The Director of the International Labour Office, in his annual report presented to the 1932 Conference, estimated the number of totally unemployed in those countries for which information of some sort was available at the end of 1931 as 20-25 millions. It is a depressing deduction from this estimate that some 60 to 70 million persons, mainly in the highly developed and richer countries of the world,

¹ For explanation of the figures quoted in each case, see successive issues of the *Statistical Year-Book of the League of Nations*.

² *Industrial and Labour Information*, Vol. XLII, No. 1.

“ are deprived of the means of existence arising from their own activity or that of those on whom they are dependent.”¹

The causes of such a situation are those which have created the period of depression and falling prices. The consequences of such widespread and persistent unemployment, on the other hand, particularly the diminished purchasing power of such large numbers of people and the very heavy costs (diminishing the purchasing power of other classes of the community) which are involved in unemployment and poor relief, form a powerful factor in the continuance and deepening of the depression. From any point of view, unemployment is the most distressing social problem of the present day. It carries with it the risk of deterioration of skill and morale, of lowering the vitality and hindering the education and industrial training of large numbers of the people of every country. Unemployment is now on such a scale that this risk threatens not only adults but young persons and, through the privation of their parents, young children. The cost of alleviating distress and minimising these risks of deterioration is a heavy burden on the budgets of most countries ; but the social consequences of reducing that burden, both in the positive deterioration of economic quality and in the discontent engendered by misery, are sufficiently clear to forbid much budgetary reduction.

In the countless proposals for positive action to remedy the depression, the spectre of unemployment is equally important. In this connection, it is perhaps sufficient to quote the considered conclusion of a recognised expert on the whole question of unemployment and its relief, repeated in 1930 after a second survey of the problems first studied twenty-one years earlier:² “ Unemployment remains, in 1930 as in 1909, a problem of industry, not an act of God The problem of unemployment — this is a point that cannot be too strongly emphasised — is insoluble by any mere expenditure of public money. It represents not a want to be satisfied but a disease to be eradicated. It needs not money so much as thought and organisation. The repeated lesson of twenty-one years since those words were penned is how much more abundant is money than thought, how much harder it is, for the cure of social ills, to change men’s habits and open their minds than to slit their purses — how much harder and more important ”.

¹ International Labour Conference, Sixteenth Session, Geneva, 1932 : Report of the Director, page 15.

² W. H. Beveridge, *Unemployment : A Problem of Industry* : London. Longmans Green, 1930, page 419.

Chapter IX.

THE STRAIN ON THE PUBLIC FINANCES.

(i) THE RÔLE OF THE STATE IN ECONOMIC LIFE.

It is a commonplace that, in most countries since the war, the State and its organs of government have come to play a part of great and increasing importance in economic life. This development has many aspects, of which conscious intervention governed by economic purposes is only one. The whole trend of recent social progress has been towards the co-operation of increasing numbers of individuals and, as the scale of economic organisation has grown, the various organs of the State have almost inevitably been drawn into supervision, regulation, competition or monopolistic enterprise. The intervention of the Government in what formerly were regarded as private economic affairs has been particularly conspicuous since the war. Moreover, the growing political influence of the economically weaker classes of the community has led to expenditures on social services which have the effect of redistributing the national income.

The mere fact that so many countries have recently passed through the experience of a great war is sufficient to have concentrated a great deal of power in the hands of governmental authorities. Large public debts have been accumulated and the taxation necessary for their service, added to that for other forms of public expenditure, has rendered necessary a heavy toll upon private enterprise and private wealth.

Unfortunately, also, as the statistics summarised below show only too plainly, the expenditure deemed necessary for defence purposes remains a very heavy proportion of the total. Indeed, expenditure on defence, even before the depression set in, remained, in many countries, as large in proportion to the national income (though not in proportion to the total Government expenditure) as in the period of armed neutrality which immediately preceded the war of 1914-1918.¹

¹ Cf. Per Jacobsson, "Armaments Expenditure of the World" (reprinted from the *Economist*, "Armaments Supplement", October 19th, 1929).

Besides the still heavy expenditure on defence services and items of State expenditure which are legacies of the war, such as heavier payments for debt and pension services, there is a large and growing expenditure upon the so-called social services. These services are not always strictly defined in discussions of public finance. In particular, the cost of education is often included. It is not always easy to draw a clear distinction between such services as education, which in most countries is rendered to the whole population as of equal right, and those which are rendered to limited groups of the population for specific reasons of economic hardship, and which therefore cause a redistribution of real income. In the following discussion, except where the context indicates the contrary, the term "social services" is used in the stricter sense as defined above. Attention has already been directed to the importance of the growth of such services.¹ They have been a factor in rendering the post-war economic system more inflexible and resistant to change and have played a large rôle in the establishment of a higher standard of living for substantial classes of the people.² At this point, however, they are viewed as one element in the growing public expenditures which, on the one hand, have in many countries endangered budgetary and therefore currency equilibrium, and, on the other, have raised taxation to levels which are a serious burden upon industry.

The facts of increasing expenditure and taxation are well known, but not always easy to state with statistical accuracy. State accounts are notoriously difficult to disentangle and do not always contain the total public expenditure. The methods of presentation of the accounts differ considerably; there are general and special funds; sometimes gross and sometimes net expenditure is disclosed; and the separate accounts of public undertakings are often of great importance. In any computation of public expenditure, local governing authorities and other public bodies must be reckoned with as well as the Central Government. The financial relations of the various public bodies are very close, so that there is considerable difficulty in avoiding double counting. All these and other reasons make it extremely difficult to arrive at even an approximate notion of the proportion which public expenditure bears to the total national income. Such computations have, however, been attempted in three important countries. These are given in the following table. They must be read as significant only of the general drift of development. There is little comparability between the methods by

¹ See Chapter I, section (v).

² See Chapter VIII.

which public expenditure, on the one hand, and national income, on the other, are calculated; but the changing proportions shown for each country are significant.

Country	Unit	Year	Estimated national income	Total expenditure of all public authorities	
				Amount	Percentage of national income
Germany ¹	RM. (000,000's)	1913-14	45,700	7,178	15.7
		1925-26	65,000	14,465	22.3
		1928-29	75,400	20,801	27.6
Sweden ²	Kr. (000,000's)	1913	2,980	463	15.5
		1928	6,750	1,473	21.8
United States ³	\$ (000,000's)	1913	34,400	2,919	8.5
		1925	79,200	11,126	14.0
		1929	85,200	13,048	15.3

The importance of this table arises, not from any comparison between the three countries, which, indeed, is not legitimate, nor from the approach to accuracy of the estimates made, but from the striking similarity of movement in the final column in the case of all three countries. It is evident that a larger share of the national income in each case is passing through the accounts of public bodies. If such figures as are available for State and local expenditure in other countries are considered, the result is broadly the same.

If an attempt is made to analyse this marked increase in public expenditure relatively to national income, the results naturally differ widely from country to country. It is extremely difficult to summarise the detailed statistics, even for a few fairly similar countries, on anything like a uniform basis. Each country compiles its accounts in its own way, and the relations between different accounts vary, as do the relations between private and public activities, and between the functions of the

¹ "Die Ausgaben und Einnahmen der Öffentlichen Verwaltung, 1913-14 to 1926-27" — *Statistisches Jahrbuch des Deutschen Reichs*, 1931.

² *Statistisk Årsbok*, 1931, pages 273 and 332; *Arbetslöshetsutredningens Beträkande I*, 1931, page 142.

³ "The Cost of Government"; National Industrial Conference Board, New York, 1931, page 17.

central authority and the subordinate public bodies. To attain a sufficient degree of accuracy in the compilation therefore involves the necessity of collecting and dissecting the detailed accounts and of studying the administration of the financial system of the country concerned, in order to get clear definitions. It is possible, however, to pick out certain important types of expenditure which are common to a great number of countries, and to compare their growth in recent years. In the following sections, special attention is paid to the amounts expended on debt service, defence, war charges and social services. The statistics used in regard to debt service have recently been the subject of special study by the Economic Intelligence Service of the League, and the defence expenditure also has been carefully analysed in the same way for some years past as part of the technical preparation for the Disarmament Conference. Expenditure on social services is rather more difficult to summarise with accuracy, since the scope of such services varies considerably from country to country and is very much complicated by the fact that subordinate (local and functional) public bodies participate so greatly in this type of expenditure that, in any attempt at estimation, allowance must be made for subsidies and cross payments of various kinds. Social expenditure has, however, come to be so heavy in many countries, especially in the depression years, that some preliminary attempt to estimate its importance is necessary.

Prolonged and detailed study of the public accounts of many countries would be needed before any considered estimate of the relative importance to each other, and to the total expenditure, of each of the groups of expenditure selected for special analysis could be attempted. There is, in the first place, no common definition or classification of these items of expenditure, which cannot therefore be compared as between countries. Some examples from particular countries may, however, serve to show that these are the groups of main interest at the present time. In Germany, according to the calculation of the *Statistisches Jahrbuch*, the cost of the army and navy compared with total expenditure fell from its pre-war percentage of 25 to 4 per cent in 1928-29; but the "war burden", internal and external, rose from 0.8 to 21.6 per cent. Debt service, apart from the "war burden", was reduced by inflation from its pre-war level of 6.6 to 1.3 per cent in 1925-26, but has since risen to 4.3 per cent. The expenditure on general administration, police, justice, education, economic development, transport and public utilities — all the normal political and economic functions of the State in pre-war practice — in 1928-29 called for 45.3 per cent of the total, as against 56.6 per cent in 1913-14; but the expenditure

on social welfare has grown from 9.6 to 17.2 per cent and that on housing from 0.4 to 7.4 per cent.¹

Germany is perhaps an extreme case of the development of social expenditure; but in Great Britain the development is very marked also, and the tendency to increase is clear in most countries. A rough approximation of the relative importance of the main items of expenditure by certain Central Governments is shown in the following table. As will be made clear later, such a calculation underestimates the tendency for social expenditure to increase, since much of this expenditure is made by public bodies other than the central authority.

¹ The detailed calculations are as follows :

DISTRIBUTION OF PUBLIC EXPENDITURE IN GERMANY
(Reich, Länder, Hansestädte, Gemeinde und Gemeindeverbände).

Purpose of disbursement	R.M. (000,000's)			Percentage of total		
	1913-14	1925-26	1928-29	1913-14	1925-26	1928-29
I. General and Financial Administration	660	1,399	1,691	9.2	9.6	8.1
II (a) Police and Justice	559	1,276	1,572	7.8	8.8	7.6
II (b) Army and Navy	1,821	633	827	25.2	4.4	4.0
III. School, Science, Art, Church	1,392	2,370	3,198	19.4	16.4	15.4
IV. Social welfare	691	2,453	3,586	9.6	17.0	17.2
V. Housing	31	1,070	1,542	0.4	7.4	7.4
VI. Economic development and communications	1,018	1,454	2,224	14.2	10.0	10.7
VII. Public utilities	429	484	738	6.0	3.3	3.5
VIII. Debt service *	477	194	903	6.6	1.3	4.3
IX. Miscellaneous	36	28	26	0.5	0.2	0.1
X. War burden { Internal	62	2,022	2,315	0.8	14.0	11.1
{ External	0	1,080	2,178	0.0	7.5	10.5
Total	7,178	14,465	20,801	100.0	100.0	100.0
				Public expenditure (Percentage of national income)		
National Income	45,700	65,000	75,400	15.7	22.3	27.6

Source : *Einzelschriften zur Statistik des Deutschen Reichs*, Nr. 10. *Statistisches Jahrbuch des Deutschen Reichs*, 1931, page 459.

* For "Gemeinde" and "Gemeindeverbände" the debt service is not included here but under the proper head, with the exception of such cases where a division has proved impossible. The whole debt service in 1928-29 was R.M. 1,207 million — i.e., 6 per cent of the total expenditure. Pensions are distributed among the various branches of expenditure.

*Percentage Proportion of Main Items of Central Government Expenditure, 1913-1928.*¹

Country	Year	De- fence	Public debt			Edu- ca- tion	Social wel- fare	War bur- den ²
			Inter- est	Amor- tisation	Total ²			
Belgium	1913	27	30	2	32	9	7	—
	1925	14	21	3	29	6	7	30
	1928	10	14	17	31	7	7	29
France	1914	42	—	—	19	9	5	—
	1925	13	31	1	34	6	2	31
	1928	16	25	11	36	6	2	26
Great Britain	1912-13	52	16	4	19	5	11	—
	1925-26	19	41	7	48	1	8	18
	1928-29	17	40	10	51	1	9	14
Italy	1913-14	33	23	1	24	5	1	—
	1925-26	19	24	5	30	4	3	16
	1928-29	23	26	1	28	4	3	11

The outstanding features of this table, summary and incomplete as it must be, are the heavy expenditure on defence, the growing debt services, the heavy war burdens for such items as pensions, and the substantial social expenditures. Since, as will be shown later, much of the increased burden of debt is a direct result of the war, it is not possible, without much fuller information than is at present available, to estimate how large a proportion of the total budgets consist of the cost of war and preparation for war; but it is evident that the important groups of expenditure which have strained the public finances of most countries in the post-war period are those selected for special treatment in the following sections — namely, the burden of debt and pensions left as a legacy of the last war, the current expenditure upon defence and the cost of social services.

The statistics which have been quoted all refer to the years before the depression set in. It is important to emphasise this fact because, although budgetary difficulties were enormously

¹ Source : *Finanzen und Steuern im In- und Ausland* ; Berlin, 1930.

² Includes other public debt expenditures besides amortisation and interest.

³ War burden includes pensions, grants-in-aid, reconstruction and occupation expenditure, and other items.

aggravated by the effect of the depression, which increased the real burden of payments on account of debt, defence and social services, besides accentuating nationalist feeling, those difficulties were present before the depression and were a very real factor in the instability which lay behind it. So large a proportion of the national income was needed for what, in a strict economic view, must be regarded as unproductive expenditure that taxation remained in most countries at a very high level. It would be necessary to undertake an exhaustive investigation in each country of the nature and incidence of this taxation, and also of the change in the distribution of wealth induced by such a large increase in public debt and social services, before arriving at any considered conclusion concerning the effect of this budgetary situation upon economic enterprise and the formation of capital resources. But certain broad conclusions are almost self-evident and are widely accepted.

The first of these is that the tax burden in the aggregate has proved to be so great that in many countries it has impaired the provision of new capital for productive industry. Such a conclusion is naturally difficult to prove statistically. It is obviously dependent upon the levels of consumption maintained by the countries concerned as well as upon the methods of taxation employed and upon the manner in which the recipients of governmental expenditure employ the funds they receive. The provision of public capital may, in certain cases, compensate for the reduced accumulation of private capital; but it is widely believed that in many countries capital consumption rather than capital accumulation has taken place.

There is one important respect in which the direct effect of such heavy taxation is damaging to the accumulation of capital. In the modern economic organisation, much of the saving necessary for the replenishment and increase of capital is provided more or less automatically by the provision of reserves and capital funds on the part of the great joint-stock enterprises. The burden of taxation has been particularly heavy upon such enterprises, and their accumulation of capital has been rendered more difficult thereby. The private individuals who receive Government services or subsidies, or draw comparatively small additions to their income from interest payments, are more likely to use such receipts for increasing their consumption.

Two aspects of the taxation of large-scale enterprises are important in this connection. In the first place, the scales of taxation to which shareholders in these enterprises are subject have been graduated more steeply both by an increase of rates and also by the fact that, at higher price-levels, a large number of incomes move upward into the more heavily taxed income

groups.¹ The proportion of taxation raised by "direct" taxes upon income and property as compared with "indirect" forms of taxation rose steeply in many different countries, as the following table shows :

Income and Property Taxation as a Percentage of Total Public Tax Revenue.^{2 3}

	1913 ⁴ (Percentage)	1925 ⁴ (Percentage)	1928 ⁴ (Percentage)
United States	10.6	64.3	67.7
India	6.7	21.2	20.2
Japan	30.4	34.3	32.0
Belgium	27.1	47.3	35.5
Denmark	29.0	42.0	35.1
France	28.1	44.1	32.0
Italy	39.7	39.2	36.2
Netherlands	32.7	47.2	43.8
Norway	17.8	40.9	31.2
Sweden	21.7	30.2	27.3
United Kingdom	47.7	58.8	55.0
Australia	9.7	27.2	26.3 ⁵

The practice of double taxation when the operation of such large-scale enterprises extends to more than one country is an important factor also in limiting the free flow of long-term capital from one country to another. The problems raised in this way have been the subject of an investigation by the League, and the complexity of the issues raised is indicated in a preliminary report already published on this subject.⁶

The tendency to find in the profits of large-scale enterprises an elastic and fruitful source of heavy taxation is one of the factors which has led to the marked change in investment habits by which extensions of business tend to be financed by incurring fixed-interest debt or simply by bank advances or overdrafts rather than by issues of share capital. This is one way in which

¹ In the depression, falling prices have naturally had the contrary effect of lowering incomes in nominal value and thereby decreasing, not only the total taxable income, but the average rates of taxation paid, so that falling receipts from direct taxation have aggravated budgetary difficulties in many countries.

² Death duty is included in income and property tax.

³ Source : *Finanzen und Steuern*, Berlin, 1930.

⁴ Financial years beginning 1913, 1925 and 1928.

⁵ 1927-28.

⁶ *Taxation of Foreign and National Enterprises in France, Germany, Spain, the United Kingdom and the United States of America* : League of Nations, Geneva, 1932 (document C.73.M.38.1932.II.A).

industry has been increasingly driven "into the banks". Moreover, the accumulation of such debt obligations tends to make the price policy of such enterprises more conservative and adds appreciably to the rigidity of the price-structure.

The existence of large public debts and the periodic necessity for interest payments and conversion operations on a large scale interferes also with the smooth working of the money markets. The financial operations of the Governments tend to exercise an influence on banking policy which may not coincide with the commercial demands of the money and capital markets and may at times cause alterations in discount rates or open-market operations dictated by budgetary rather than trade or industrial considerations. Such heavy debt burdens as most European Governments carried, added to their growing expenditures in other directions, could be supported only when prices were relatively high and business was sustained by easy monetary conditions. Even then, taxation was so high that it took an increasing proportion of the national income. When prices fell and the nominal value of national incomes was reduced, the more rigid governmental expenditures became intolerable and relief had to be sought by cutting down expenditure if budgetary and, therefore, currency equilibrium was to be maintained.

There is a very real sense, therefore, in which the ultimate costs of the war lie behind the present depression. The war was fought with present resources, but the property rights created as the means whereby the various Governments obtained control of those resources remained as a mortgage upon future production. The national debts and other burdens incurred during the war were undertaken when the price-level was very much higher than it became after 1920 and still higher than it is in 1932, so that the resources actually used were less in amount than those now represented by the property claims. It is true that the recipients of income from such claims are taxed. It is sometimes argued, therefore, that the service of internal debt is not a real burden on productive enterprise, since the debt-holders are also the principal taxpayers. The existence of such debt claims, however, obscures the real impoverishment caused by consumptive war expenditure and tends to encourage further consumption which eats into capital resources. In the process of redistributing wealth, a large part of the wealth is consumed, and there has been increasing difficulty after the war in providing the real capital necessary for economic development. This difficulty was masked by credit expansion which, between 1925 and 1929, made possible the "papering-over of cracks in the structure which were none the less threatening because outwardly

all seemed to go well".¹ The plain fact is that the financial obligations which were a legacy of the war and the disturbance of economic organisation which their service entailed were largely responsible for the budgetary strain which led to financial and economic insecurity and to policies which, in postponing, aggravated the necessity for fundamental readjustment of public debts, national and international.

(ii) THE INCREASED BURDEN OF PUBLIC DEBT.

The increased burden of public debt in the post-war period is only partly indicated by the statistics which show, for the various countries concerned, the growth of total debt.² The growth of public debt is primarily important, because, in return for current expenditure, public bodies contract a liability for future annual payments on account of debt service. These payments may be assured by current receipts from the assets created by the expenditure of loans, or they may need to be collected by taxation. It is the annual payments on debt service in relation to the receipts from public assets created by loan expenditure which present the significant problem. Moreover, there is not a clear correlation in every case between the aggregate of public debt and the annual payments on account of debt service, since floating debts may include arrears of payments for services rendered or goods delivered, but the debt service will not include payments on such arrears. Each loan transaction, as a rule, is complete in itself with its own arrangements concerning security, interest, sinking fund, issue price, priority, redemption and other details. The aggregate figures obtained by adding the nominal amounts of various loans outstanding cannot give an adequate indication of the complexity of the problem or the budgetary difficulties to which it gives rise. In calculating any such aggregate, it is obviously necessary to take account, not only of the debts of the Central Governments, but also of those incurred by the subordinate governing authorities. This is especially important in the post-war period, since there has been a great expansion of borrowing on the part of municipalities and other public bodies in many countries, an expansion largely caused by the increased demand for social services. The distinction between debt service payable within a country and that payable abroad is also important, since it affects the balances of international payments.

¹ *Economist*, June 11th, 1932.

² League of Nations *Statistical Year-Book*, 1931-32, pages 254 to 258.

Moreover, in the post-war period, there has been a noticeable multiplication and complication of debt charges of an unusual character. In addition to the more usual form of borrowing by which Governments raise loans from private individuals and institutions, there is a very heavy burden of inter-governmental indebtedness and of reparation payments. In the main, these inter-governmental transactions are a legacy from the war period.

They fall into two groups—reparation obligations and inter-Allied debts. The first group consists chiefly of Germany's general reparation obligations to the Allies, together with her separate obligations to Belgium under the Mark settlement, to the United States under the German-American debt agreement, and to Roumania under the agreement of March 31st, 1929, as well as the reparation obligations of Hungary and of Bulgaria, and the "Liberty" obligation of Czechoslovakia. Of these, the first item is the largest and most important.¹

The inter-Allied war debts are also made up of a great number of complicated transactions. They may perhaps best be represented by the two following tables giving the statistics concerning the debt settlements made respectively by the United States and Great Britain with their various debtors.

¹ *Wochenberichte des Institutes für Konjunkturforschung*, January 13th, 1932. See also "Reparations and War Debts", Supplement to the *Economist*, January 23rd, 1932.

Table showing the Sums due to the United States of America by the Various Foreign Governments on Account of Principal at the Date of the Respective Funding Agreement, and the Amount of Interest and Amortisation paid from July 1st, 1930, to June 30th, 1931.¹

Country	Date of Funding Agreement	Principal	Annuity paid from July 1st, 1930, to June 30th, 1931		
			Interest	Amortisation	Total
		\$ (000,000's)		\$ (000's)	
1. Armenia ²	—	12.0	—	—	—
2. Austria	January 1st, 1928	24.6	—	287.5	287.5
3. Belgium	August 18th, 1925	417.8	3,250.0	4,050.0	7,300.0
4. Czechoslovakia	October 13th, 1925	185.1	—	3,000.0	3,000.0
5. Estonia	October 26th, 1925	13.8	397.0	—	397.0
6. Finland	May 1st, 1923	9.0	258.9	55.0	313.9
7. France	April 29th, 1926	4,025.0	38,650.0	1,350.0	40,000.0
8. Great Britain	June 18th, 1923	4,600.0	132,360.0	28,000.0	160,360.0
9. Greece	May 10th, 1929	30.3	466.2	484.0	950.2
10. Hungary	April 25th, 1924	1.9	57.4	11.8	69.2
11. Italy	November 14th, 1925	2,042.0	2,521.3	12,100.0	14,621.3
12. Latvia	September 24th, 1925	5.8	153.3	—	153.3
13. Lithuania	September 22nd, 1924	6.0	187.1	37.5	224.6
14. Nicaragua ²	—	0.3	—	—	—
15. Poland	November 14th, 1924	178.6	6,173.4	1,287.3	7,460.7
16. Roumania	December 4th, 1925	66.6	—	700.0	700.0
17. Russia ²	—	192.6	—	—	—
18. Yugoslavia	May 3rd, 1926	62.9	—	225.0	225.0
Total	—	11,874.3	184,474.6	51,588.1	236,062.7

¹ Source : Annual reports of the Secretary of the Treasury on the state of the finances for fiscal years ended June 30th, 1930, and June 30th, 1931.

² Funding Agreement has not been reached.

Table showing the Sums due to Great Britain by the Various Foreign and Colonial Governments on Account of Principal at the Date of the Respective Funding Agreement, and the Amount of Debt Service paid from April 1st, 1930, to March 31st, 1931.¹

Country	Date of Funding Agreement	Principal £ (000's)	Amounts paid from April 1st, 1930, to March 31st, 1931 £ (000's)
War Loans :			
Loans to Domini- ons and Co- lonies :			
Australia . . .	1921	196,750	5,549
Newfoundland		1,082	21
New Zealand .	September 6th, 1922	62,158	1,746
South Africa .		18,847	337
Crown Colonies and Protec- torates . . .		1,523	31
Total . . .		280,360	7,684
Loans to Allied Powers :			
France	July 12th, 1926	799,500	12,500
Greece	April 9th, 1927	23,550	300
Italy	January 27th, 1926	254,550	4,000
Portugal	December 31st, 1926	23,975	350
Roumania	October 19th, 1925	31,250	250
Yugoslavia . . .	August 9th, 1927	32,800	300
Total		1,165,625	17,700
Loans for Relief, Reconstruction, Repatriation, etc.:			
Austria		9,130	107
Belgium	December 31st, 1925	18,148	450
Belgian Congo .	December 31st, 1925	7,252	180
Czechoslovakia .		1,583	106
Estonia		2,217	70
Greece		108	11
Latvia		2,300	75
Lithuania		165	33
Poland		7,236	569
Roumania	October 19th, 1925	3,748	212
Yugoslavia		3,093	151
Total		54,980	1,964
Grand Total		1,500,965	27,348

¹ Sources : British official (Cmd.) papers, and *Die interalliierten Schulden, ihre Entstehung und ihre Behandlung im Youngplan* (Statistisches Reichsamt), 1930.

The total effect of such a network of annual payments as is involved in the settlement of reparation payments and war debt service is not easy to summarise statistically. The following table shows the amounts which various countries were liable to pay or had a claim to receive during 1931-32, when the Hoover moratorium went into force on July 1st, 1931.

*Financial Effect of the Hoover Moratorium.*¹

Government of	Suspended receipts	Suspended payments	Net loss (—) or gain (+)
		£ (000's)	
United States	53,600	Nil	— 53,600
Great Britain ²	42,500	32,800	— 9,700
France	39,700	23,600	— 16,100
Italy	9,200	7,400	— 1,800
Belgium	5,100	2,700	— 2,400
Roumania	700	750	+ 50
Yugoslavia	3,900	600	— 3,300
Portugal	600	350	— 250
Japan	600	Nil	— 600
Greece	1,000	650	— 350
Canada	900	Nil	— 900
Australia	800	3,900	+ 3,100
New Zealand	330	1,750	+ 1,420
South Africa	110	(340)	— 110
Egypt	90	Nil	— 90
Germany	Nil	77,000	+ 77,000
Hungary	Nil	350	+ 350
Czechoslovakia	10	1,190	+ 1,180
Bulgaria	150	400	+ 250
Austria	Nil	300	+ 300

It is obvious that such large non-economic payments have complicated the balancing of international accounts in recent years. Not only are the amounts involved very large in the aggregate, but the transfer problems raised by such transactions seriously complicate the operations of the money markets and add a very confusing element to the forces which maintain the

¹ *Economist*, Supplement, *op. cit.*

² The British debit balance is accounted for by the war debts of the Dominions, reconstruction debts and other items excluded from the scope of the Balfour Note.

delicate equilibrium of the various national price-structures. The network of financial transactions involved in the service of war debts and in the equally complicated provision and distribution of reparation payments has exercised an abnormal influence on the processes by which the international exchange of commodities and transferences of capital are determined.

In addition to such inter-governmental transactions, however, there was, in most countries, a very great increase in the public debt, both internal and external, which resulted from war expenditure. Any thorough and accurate study of this question would involve separate consideration of the circumstances of individual countries, and it is impossible in any brief space to summarise the statistics.

The growth of war debt was not confined to Europe or to the belligerent countries. The public debt of Canada, for example, was multiplied eightfold in the war years; Australia and New Zealand, the most remote countries from Europe, incurred heavy obligations also; and, indeed, there was a general world tendency to a rapid increase of debt burdens.¹ Even the neutral countries were in many cases forced to undertake heavy expenditure and to increase their debts, not only because they maintained their defence services in a state of readiness for war, but also because the State undertook new functions and, in particular, intervened to support banks and private institutions the stability of which was disturbed by the dislocations of the war period.

In some of the stronger financial countries, particularly those which were creditors on balance, there were substantial reductions of the total public debt in the first post-war decade. The outstanding example is that of the United States, which reduced its total debt from \$25,482 million at June 30th, 1919, to \$16,185 million at June 30th, 1930.² Canada also reduced her debt from \$3,041 million in 1920 to \$2,545 million in 1930.³ In Great Britain, France and Belgium, the reductions were less substantial. The total British debt was £7,876 million on March 31st, 1920, and had fallen to £7,583 million on March 31st, 1931; the French debt fell from 492,938 million francs in 1926 to 480,821 million francs in 1931 (March 31st); while the Belgian debt was reduced from 58,343 million francs at the end of 1925 to 52,413 million francs at September 30th, 1931. The reduction

¹ There were notable exceptions, as, for instance, in the case of Japan, where the international financial position improved materially at this time. Cf. H. G. Moulton, *Japan*; Washington, Brookings Institution, 1931, Chapter XII.

² The debt increased again to \$16,801 million in 1931 and also in 1932.

³ \$2,610 million at March 31st, 1931.

of the real burden of public debts which resulted from inflation, in a number of countries, was very much more substantial than the repayments mentioned above, but cannot be measured precisely. On the other hand, there is a long list of countries — most of the rest of the world, in fact — where the burden of indebtedness has steadily increased. It is difficult to make any general statement about this widespread tendency to increased borrowing in the post-war period. A certain proportion of the loans contracted in practically every country was for reproductive purposes. In Europe, reconstruction loans were floated from 1924 onwards in order to facilitate currency stabilisation; in both Europe and the oversea borrowing countries there was borrowing on a large scale for public works and projects of economic development.

While any general statement must be made with great caution and hedged about with qualifications in particular cases, there seems little doubt now that the amount of borrowing in the aggregate, for most countries and for the world as a whole, was excessive in the years 1925-1929, and made possible only by credit expansion. Moreover, under the system of industrial financing by bank advances, many loans to private businesses recoiled first upon the banks which were interested in the debtor industries and, in some cases, ultimately upon the State.

The post-war world, in fact, became entangled in a network of indebtedness which constricted economic activity. The fundamental instability of this situation was revealed, after the large volume of foreign lending began to dwindle in 1928-29, in a growing disparity in interest rates between the money markets, on the one hand, of creditor and, on the other, of debtor countries. By the middle of 1929, the yields of bonds were diverging in alarming fashion.¹ As will be shown in a later section of this chapter, this divergence was greatly aggravated as the depression proceeded.

Some of the strong creditor countries were assisted in their policies of debt reduction by opportunities of conversion lowering the burden of interest payments, and also by opportunities of purchasing securities for redemption.

The high rates of interest which ruled in the war period, when so large a proportion of the debt of most countries was actually incurred, have, however, raised the average rate of interest payable on the aggregate of debt to a much higher figure than was customary before the war. To take only one example, the war debt of Canada bears interest at an average rate of 4.992

¹ *Course and Phases of the World Economic Depression*, page 210.

per cent, as against an average rate of 3.52 per cent for the pre-war debt.

Apart, therefore, from the important effect of such heavy burdens of governmental indebtedness in disturbing the normal operations of the money markets, the post-war world was burdened with a precarious budgetary situation in almost every country, created in large part by the necessity of providing so large a proportion, not only of the Government receipts, but of the national income for debt service. The serious nature of this drain on the national income of several important countries is shown in the table below :

*Governmental, State and Local Debt Service.*¹

(National Currency (000,000's omitted).)

Year	Country	Estimated national income	Total public expenditure	Debt service	Debt service as a percentage of	
					National income	Total public expenditure
1925 ...	Belgium	31,000 ²	8,331	2,388	7.7	28.7
1928-29	Germany	75,400	13,601 ³	829 ³	1.1 ³	6.1 ³
1925-26	Italy	90,000 ²	22,295	5,024	5.6	22.6
1925-26	United Kingdom	4,150	1,083	382	9.3	35.4
1929 ...	United States	85,200	13,062	2,607	3.6	20.0

¹ Sources :

Belgium : *Finanzen und Steuern*, Berlin, 1930, page 596. Bauduin : " Le Revenu national en 1930 ". *Bulletin d'information et de documentation*, 25 mai 1930.

Germany : *Statistisches Jahrbuch für das Deutsche Reich*, 1931, pages 457 and 485.

Italy : *Finanzen und Steuern* : Berlin, 1930, pages 607 and 667.

United Kingdom : *Finanzen und Steuern*, Berlin, 1930, page 575. *Economist*, Budgetary Supplement, April 1930.

United States : *Cost of Government 1929-30*. Washington, 1931. Of the total debt service, \$1,124 million were used for amortisation.

² 1927.

³ Reich, Länder und Hansestädte only. Debt of local authorities was, at March 31st, 1929, 9,940 million RM., while the debt of Reich, Länder und Hansestädte amounted to 11,930 million RM. at the same date, not including reparation payments.

Certain further comments are necessary in regard to the table. The statistics are not comparable between countries, since the estimates of national income are not compiled on a uniform method. Moreover, payments on account of foreign war debt service began at different dates. The Belgian and Italian debt settlements came into force in 1926, so that the figures shown above do not disclose the present position. The effect of the British settlement with the United States, which came into effective operation in 1924, is shown clearly.

During the years 1924-1929, compositions and settlements in regard to war debts, as well as reparations, followed one another until a complicated system of payments, which in the aggregate were very large, was built up. These payments seriously disturbed the balances of international payment, particularly since the transfers of goods rendered necessary by them were hampered by increasing tariff restrictions. Large capital movements made it possible to make the payments for a few years; but, when the flow of capital dwindled in 1928-29, the aggravated transfer difficulties that ensued caused a collapse, first of prices and then of international trade.

The fall in prices, in turn, made the burden of debt payments very much heavier, and, as the depression worsened and transfer difficulties became greater, the adjustment of international debts was more and more obviously necessary.

(iii) EXPENDITURE ON ARMAMENTS.

Prolonged and intricate technical discussions by budgetary experts at the Disarmament Conference and its Preparatory Commission have shown how difficult it is to establish in accurate detail comparable statistics of expenditure upon armaments. The definition of armaments is not a simple question. There are great differences between the organisation of defence in various countries, between the systems of accounts, and between the levels of prices, salaries and wages. But, if comparisons between the expenditures of different countries are difficult, this is not equally true of comparisons of the expenditure in each country at different periods. The information supplied by the various Governments for the purpose of the Disarmament Conference,¹ while not complete and uniform in all cases, is

¹ Cf. *League of Nations Armaments Year-Book* (Special Edition), Geneva, 1932, and the series of Disarmament Conference documents which contain the fuller information supplied by the various Governments for the purpose of the 1932 Disarmament Conference.

adequate enough to show beyond doubt that the cost of preparation for possible war is a heavy burden on national budgets, in most cases as heavy a burden as in the pre-war period (absolutely but not always relatively to the increased governmental expenditures). It is, moreover, in many cases an increasing burden.

It has been shown that the proportion of the budgets of European States which is attributable to past wars and to the possibility of future wars is in some cases (*e.g.*, France and Great Britain) as high as 70 per cent.¹ Comparison in this respect with the United States is not possible, because the scope of the federal budget is more limited and a greater proportion of governmental expenditure is incurred by the States. Moreover, it is no longer possible in the modern world to confine war and preparation for war within narrow limits. The heaviest cost lies in the check to international economic co-operation which arises from war, its preparation and its aftermath. There are certain countries which have enjoyed a long period of peace. Sweden and Switzerland, for example, have not been engaged in war for over a hundred years. In these countries, however, the indirect cost of war, even to neutrals, is reflected in heavy debt charges, a large part of which was incurred in the last European war. The destructive efficiency with which modern warfare is waged and the necessity for extending its preparation and conduct into every aspect of economic and social life leave no country unscathed.

A comparison with pre-war levels of expenditure, even allowing for the higher level of prices ruling before the present depression, shows that, with the exception of Germany, current armament expenditure in most cases tends to reach, and in some cases to exceed, the pre-war rate. Reductions of expenditure up to 1930 were not nearly as great as the fall in the purchasing power of money in the depression. The maintenance of armament budgets at their present levels therefore means a substantial increase in the real as distinct from the nominal budget. There is a strong economic case for reduction because of this fact alone.

(iv) THE COST OF SOCIAL SERVICES.

The increasing cost of social services, as distinct from the older administrative activities of public bodies, was a substantial

¹ Per Jacobsson, "Armaments Expenditure of the World" (reprinted from the *Economist*, "Armaments Supplement", October 19th, 1929).

cause of budgetary difficulties in many countries even before the depression set in during the latter part of 1929. The definition of social services varies in current literature. In particular, such services as education, rendered, at least in theory, to the whole community, are sometimes included. The line is difficult to draw; but there is a distinction between expenditure upon such items as education and that upon services rendered or payments made to particular classes of people as compensation for economic hardship. There is a general tendency, as productivity increases and standards of living rise, for education and similar services to be improved. In addition, as the political power of democracies is exercised, an increasing number of social services, strictly defined, are undertaken by public bodies. These are not always clearly distinguished, as when provision for the feeding or medical care of schoolchildren is made by educational authorities.

In the strict definition of the term, social services include housing schemes; provision for protection and compensation of workers; old-age, invalidity and widows' pensions; family allowances; unemployment, health and accident insurance; poor relief; and similar governmental activities. There has been a marked extension of such services in recent years, but social insurance may be traced back to the reform programme initiated by Bismarck in Germany during the 'seventies; old-age pensions were first introduced in Denmark in 1891, and New Zealand initiated a policy of wage regulation in 1894.

Many of the schemes introduced to safeguard the economically weaker members of the community involve contributions from employees, or workmen, or from other recipients. Such pension schemes as those which apply to civil and other public servants should properly be regarded as part of the cost of administration. War pensions should be classed as part of the war burden of the country concerned. In so far as contributory schemes — for example, of various kinds of insurance — are independent of State subsidies, they cannot strictly be classed as social services. But the tendency is for the public expenditure on such services to increase, and to cause a considerable redistribution of income from taxpayers to the recipients of public expenditure.

Comparable statistics of social expenditure in different countries are not at present available.

The statistics for Germany have been calculated as follows :

*Public Expenditure (including State and Municipal Grants)
on Education, Social Welfare and Housing.*¹

	1913-14	1925-26	1928-29
	RM. (000,000's)		
Education	1,392	2,370	3,198
Social welfare	691	2,453	3,586
Housing	31	1,070	1,542
Total public expenditure . . .	7,178	14,465	20,801
Estimated national income . .	45,700	59,900	75,400

	1913-14	1925-26	1928-29
Social Welfare and Housing :			
(a) As a percentage of total public expenditure	10	24	25
(b) As a percentage of national income	1.6	5.9	6.8

The magnitude of the problem is clear from the percentages quoted above, which are an understatement, since there are large contributions by employers and employees to social insurance which do not pass through the public accounts. These have been estimated as rising from 2.5 per cent of the national income in 1913 to 7.4 per cent in 1929.²

In Great Britain, the increase of expenditure on social services has also been great. The sums spent in England, Scotland and Wales from local rates, parliamentary grants and other receipts, such as unemployment contributions, rents, fees, etc., were calculated by the *Economist* as follows :³

¹ *Einzelschriften zur Statistik des deutschen Reichs*, Nr. 10, and *Statistisches Jahrbuch*, 1931, pages 459 and 532.

² *Finanzen und Steuern*, Berlin 1930, page 550.

³ *Economist*, "Budget Supplement", April 9th, 1932.

	Year ending March 31st				
	1921	1924	1928	1929	1930
	£ (000,000's)				
Unemployment insurance	10.8	48.0	42.8	53.8	53.3
Health insurance	29.9	30.9	37.6	39.9	38.6
War pensions	100.9	69.6	56.9	54.0	51.4
Other pensions	20.8	24.0	45.6 ¹	58.7 ¹	62.2 ¹
Education	88.8	86.6	94.4	97.0	100.5
Working-class housing	4.7	16.6	26.7	31.6	35.6
Poor relief	34.3	41.9	45.5	43.9	45.0
Miscellaneous ²	16.5	14.5	16.5	16.9	17.4
Total	306.7	332.1	366.0	395.8	404.0
Total (less war pensions and education)	117.0	175.9	214.7	244.8	252.1
Total, less war pensions and education, as a percentage of national income ³	.	4.2	5.1	5.6	6.3

In France, Belgium, Italy and the United States, the proportion of public expenditure (and of national income) devoted to the social services is much less than in Germany or Great Britain, but has tended to increase in the depression period.

In many of the newer countries, particularly Australia and New Zealand where the social movement gained striking successes in the last generation, the increased cost of social services has also been noticeable. In both Australia and New Zealand, the depression has caused substantial reductions in educational expenditure, old-age pensions and other social services.

The report of the British Committee on National Expenditure (the May Committee) published in July 1931⁴ drew attention, in a series of striking introductory paragraphs, to certain urgent problems of Government expenditure and parliamentary control

¹ Includes widows', orphans' and old-age contributory pensions under the Act of 1926.

² Including expenditure on hospitals, maternity and lunacy.

³ This table is not comparable with the preceding table showing German statistics.

⁴ Cmd. 3920.

over financial commitments. Services financed by loans or by subsidies based on loans pile up subsidy obligations for the future, so that, "even if the services were immediately closed down, the taxpayer must continue for many years to provide large sums annually to liquidate past commitments". In much the same way, civil service pensions involve liabilities which do not fully emerge until many years after the legislation is enacted. The comparatively light expenditure in the initial stages of schemes for old-age and widows' pensions tends to be met in the same way from current revenue as they fall due, instead of being provided for by the setting aside each year of amounts fully equal to the actuarial liability incurred.¹

There is a marked tendency towards a rapid growth of commitments which become progressively more burdensome, but which cannot easily be reduced. Whatever view is taken of the justice of the expenditure in itself, there is an evident need for caution in the methods by which liabilities are appraised before legislation is passed.

Since existing legislation has created large and increasing liabilities in many countries, it is clear that a temporary reduction of rates of expenditure is not a final solution of the problem. The May Committee reported that "only with an increasing revenue can we continue to provide even our existing services without additional taxation". It is probable, therefore, that the problem of the social services will remain a storm centre of controversy for some time to come. The conflict of social philosophies that lies behind the controversy has been developing for many decades and will remain a central problem in social politics long after the immediate stress of the present financial depression has passed into history.

(v) The EFFECTS OF THE DEPRESSION UPON
BUDGETARY STABILITY.

The preceding sections of this chapter have dealt largely with the budgetary strain that developed before the depression set in and was, indeed, an important cause of the depression. When prices fell steadily during 1929 and precipitously after October of that year, the strain was greatly aggravated. The disorganisation of production and trade which followed made the budgetary position in nearly every country still worse, so that the depression became a further cause of budgetary disequilibrium.

¹ *Ibid*, Paragraphs 11 to 18.

Moreover, the heavy taxation burdens rendered necessary are a real obstacle to recovery.

The sequence of causation is very clear. The first effects of depressed conditions of trade are felt in a pressure for increased governmental expenditure, especially on the social services. But falling prices and diminished trade soon reduce tax receipts, while the cost of debt services and other forms of expenditure which are fixed by contract in terms of money remain at their former level. Income taxation as a whole falls off as profits diminish and incomes are reduced ; the revenue from Customs and excise duties declines as trade decreases and unemployment spreads, and there is an all-round shrinkage of receipts. Deficits appear and must be met either by fresh taxation, by public economy, or by borrowing. It requires not only public spirit but some elasticity in the tax system to raise adequate amounts of fresh taxation in a time of trade depression, but in many cases elasticity had been strained almost to breaking-point by heavy and long-continued taxation. Public economy, on the other hand, is difficult of achievement. Resolute and strong Governments in countries which still have financial reserves may achieve both higher taxation and reduced expenditure. The immediate post-war experiences of inflation are still vivid in the social memory of many countries, and therefore the most determined efforts have been made and are still being made to maintain balanced budgets. But in many cases such a balanced position rests upon moratoria which give temporary relief from important items of expenditure.

In the following table, the total receipts and expenditure during the years 1929-30 and 1930-31 are given for a number of countries for which closed accounts are available.

Summary of Budget Accounts.
Closed Accounts.

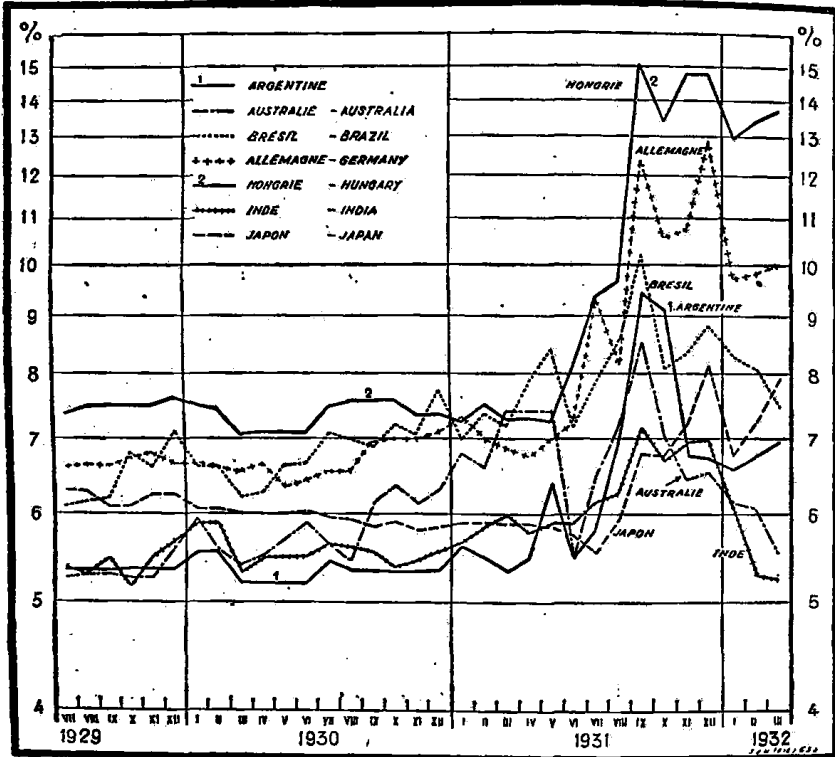
		1929-30			1930-31		
		Rev- enue	Expen- diture	Bal- ance	Rev- enue	Expen- diture	Bal- ance
		(000,000's)					
South Africa . . .	£	61	73	— 12	57	71	— 14
Canada	\$C	449	393	+ 56	357	435	— 78
United States . . .	\$	4,174	3,994	+ 180	3,317	4,220	— 903
Brazil	Milreis	2,341	2,224	+ 117	1,757	2,583	— 826
India	Rupee	1,405	2,046	— 641			
Japan	Yen	1,536	1,736	— 200			
Germany	RM.	10,641	11,352	— 712	10,655	11,740	—1,085
Austria	Schilling	2,075	2,027	+ 48			
Bulgaria	Lev	6,713	10,449	—3,736	5,655	6,946	—1,290
Denmark	Krone	379	371	+ 8	395	394	+ 1
Spain	Peseta	3,725	4,056	— 331	3,735	3,697	+ 38
Estonia	Kroon	91	96	— 5	90	97	— 7
France	Franc				50,988	53,630	—2,642
Greece	Drachma	9,951	18,363	—8,412	10,220	11,180	— 960
Hungary	Pengö	1,480	1,479	+ 1			
Italy	Lira	20,355	20,790	— 435	18,647	20,060	—1,413
Norway	Krone	377	396	— 19			
Holland	Gulden	847	914	— 67			
Poland	Zloty	3,029	2,993	+ 36			
Portugal	Escudo	2,086	2,062	+ 24	2,059	1,919	+ 137
Roumania	Leu	36,018	34,372	+1,646			
United Kingdom	£	815	840	— 25	858	892	— 34
Sweden	Krone	784	811	— 27	791	819	— 28
Switzerland	Franc	441	419	+ 22	577	570	+ 7
Czechoslovakia . . .	Koruna	10,444	10,275	+ 169	9,654	9,928	— 275
Australia	£A.	103	170	— 67	94	176	— 82
New Zealand	£N.Z.	57	104	— 46	40	97	— 57

The diagrams which follow show the movement of bond yields in various countries. The strong upward movement which developed in many countries, particularly after the third quarter of 1931, is an indication of the low prices to which Government bonds had fallen in those countries as a result of the fear of currency difficulties.

Actual Percentage Yield of Bonds. ¹

A. According to London Quotations.

(Logarithmic scale.)

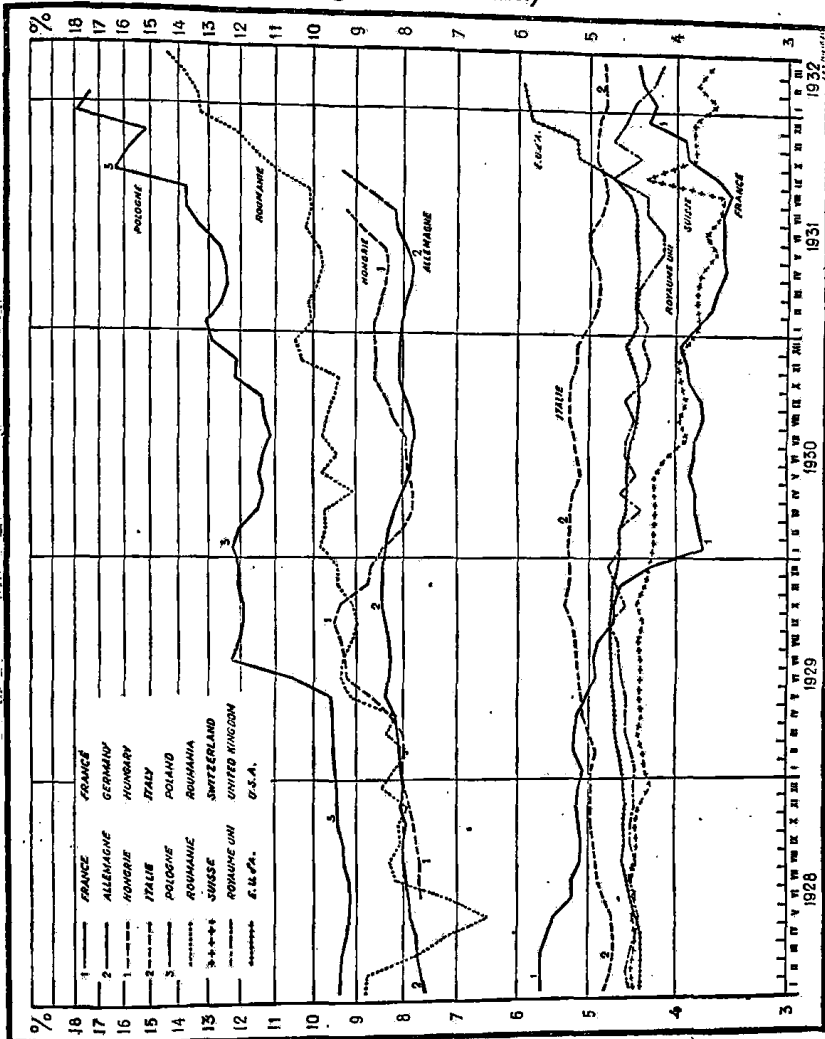


Argentine: 4 % Rescission.
 Australia: 5 % Registered.
 Brazil: 5 % Funding 1914.
 Germany: 7 % 1924
 (Dawes).

Hungary: 7½ % 1924.
 India: 3½ % Government
 stocks.
 Japan: 6 % 1924.

¹ Balances of Payments 1930, Geneva, League of Nations, 1932, page 35.

Actual Percentage Yield of Certain Bonds or Groups of Bonds.
 B. According to Domestic Quotations.¹
 (Logarithmic scale.)



- France : Miscellaneous bonds.
- Germany : Miscellaneous bonds, 8 % and less.
- Hungary : Forced Loan 1924, 5%.
- Italy : *Rentes*, 3½ %.
- Poland : Government bonds.

Roumania : Government bonds.
 Switzerland : Railway bonds.
 United Kingdom : Consols, 2½ %.
 United States of America : 60 miscellaneous high-grade bonds.

¹ *Ibid*, page 36.

These diagrams clearly reflect the investors' appreciation of the difficulties being experienced by many countries in balancing their budgets. Those countries which experienced difficulties in transferring the credits due for external payments, even though their budgets were balanced in terms of their national currencies, are in an even worse position.

As these lines are being written, the Lausanne Conference is meeting in its first sessions. The international financial situation in all its gravity is to be the subject of consideration by the responsible statesmen of all the principal Powers concerned, with the exception of the United States. Plans for aid to those countries the financial position of which is most immediately threatened have been carefully prepared and linked with wider schemes of economic restoration. Upon the decisions taken in regard to such plans hang, not only the solvency of the countries immediately concerned, but the possibility also of avoiding a further serious aggravation of the financial depression, with all the consequences that such an aggravation might entail.

While no one would deny or minimise the importance of securing international agreements, especially in regard to measures designed to relieve those countries which are suffering by reason of the difficult transfer problem, it is obvious that a firm and prudent control of public finance is also necessary. In so far as the difficulties of transferring external payments arise indirectly from concealed budgetary weaknesses in the debtor countries, their permanent solution can be found only by reductions of public expenditure. Even in the stronger creditor countries, as the bond yields for the United States and France bear witness, the prospect of large deficits causes alarm. Recovery from the depression is dependent, *inter alia*, upon such readjustments of public expenditure and taxation as will assure equilibrium in the public finances, allay the fears of investors, avert further violent movements of short-term credit balances, and, above all, afford the possibility once again of capital accumulation in place of capital consumption.

Chapter X.

THE DEVELOPMENT OF COMMERCIAL POLICY.

(i) THE SIGNIFICANCE OF INTERNATIONAL TRADE.

The rapid and cumulative growth of international trade in the modern world is primarily the result of scientific discovery and the mechanical inventions and commercial organisation based upon it. Between 1900 and 1928, it has been estimated that the total value of recorded world trade rose from \$21,000 million to \$66,700 million, and, even if allowance is made for the different levels of prices and for the fact that there were more countries recording at the latter date, the *quantum* of commodities transferred probably doubled in this period.¹ With this increase of commodity trade has gone a greatly increased volume of international capital movements. The economic and social importance of these developments may be seen, not only in the interdependence of the modern world, but equally in such social consequences as the disruptive influence which has been exerted in ancient civilisations like those of Asia, and in the settlement and rapid progress of the newer countries of North America and Oceania.

Such a strongly marked tendency towards increasing international economic co-operation provides the clearest possible example of the importance of considering the background of economic fact against which economic and political policies must be administered. The impetus of the forces which are responsible for this tendency is by no means spent. Individual trading initiative is still powerful, and the network of international trade and finance which it creates becomes increasingly important. Indeed, the progress of the natural sciences constantly opens

¹ *Europe — United States*, Vol. 2 : "Development of Trade and Capital, their Distribution and Competitive Conditions between the Two Areas since 1900", page 10, International Chamber of Commerce, 1931.

up new vistas of change, as, for example, in aerial transport and electrical communication.

Moreover, increasing ease, certainty and cheapness of communication tends in itself to break down the disparities between social organisation in different areas. Standards and manners of living tend to approximate more to a single world pattern. There still remain enormous differences between the economic and social life of different countries, but the consciousness of these differences is steadily increasing. New inventions rapidly become universalised. Motor vehicles, safety-razors, electric elevators, and a host of similar modern inventions are universally advertised and desired. Exotic products, such as tea, silks, coffee, cocoa, introduced first as luxuries, rapidly become necessities of civilised life, and demand for them is insistent upon not only cheapness but regularity in bulk supply. Specialisation of industrial production has created the huge international trade in "tonnage" minerals, foodstuffs and raw materials, while equally promoting the reverse flow of manufactured products. The improvement of productive processes becomes dependent also upon the rarer "poundage" minerals and raw materials — tungsten, antimony, aluminium and their like. There has been, in fact, an irresistible pressure towards international economic co-operation. A large part of the history of the nineteenth and twentieth centuries is connected with this pressure, as new lands were opened up, not in the search for fugitive, easily procured wealth, but with the double object of securing sources of raw materials and markets for finished products. Nor was this pressure confined to comparatively empty or weakly populated lands. The densely peopled ancient civilisations of Asia have equally been drawn into the world economy which is in process of creation by the initiative of traders.

The more irregular development of international trade since the war and the commercial policies built up to cope with its fluctuations must therefore be viewed against a background of increasing interdependence. That interdependence of the peoples of the world has received growing recognition; but against it must be set the immensely powerful and important forces of nationalism. The contrast is not simply that between economic forces promoting internationalism and political, social or cultural motives for the preservation of national unities, so much as between different conceptions of social life and progress. Not all the economic forces foster international development. There are, indeed, powerful economic motives which work against it. At the same time, the political and social philosophy of world unity opposes itself increasingly to the conception of national cultural sufficiency.

The great problems of commercial policy, national and international, are deeply rooted therefore in the realities, not only of economic activities, but equally of social philosophies. It is perhaps for this reason that the mid-nineteenth-century movement towards universal free trade was quickly checked. The "calico millennium", forcibly as its advantages impressed contemporary Europe, was far from winning universal support even in the first flush of its early triumphs. The same conflict has lain behind the indecision of commercial policy in the post-war world.

The fact of interdependence among the nations has, indeed, become clearer. The creation of an increasing number of institutions — legal, political, financial, commercial — to deal with the international relations of a rapidly changing world is clear evidence of this. But the pace of economic development has accelerated, and with it the scale and rapidity of social change is greatly increased. In the stricken, disorganised post-war world, on the other hand, stability of economic and social organisation appeared very desirable. Nations faced with immense problems of reconstruction, or, in the case of new political units, of construction, in every aspect of their organised life, were not well placed to cope with the drastic readjustments entailed in the free and unhampered development of international trade. Peasant communities in Eastern Europe found the wheat production which was one of their economic bases imperilled by imports of cheaper wheat produced by machine methods in the large-scale farming enterprises of the New World. The establishment, re-establishment or maintenance of manufacturing production in many countries encountered equally formidable competition. At every turn, the reintegration of the post-war world seemed to involve great and difficult rearrangements of productive organisation.

On the other hand, retreat to the simpler, more stable forms of national economy involved the risk, not only of losing the advantages of specialisation, but of throwing into disorder the already intricate network of international finance. The regular supply of exotic commodities which have now become necessities either for consumption or for industrial production, the maintenance of sufficiently large markets to make possible standardised production of manufactured goods on a large scale, all the processes of territorial division of labour, have come to support levels of living which are impossible of attainment without such international co-operation.

The problem of commercial policy in the post-war world, therefore, is one of securing these advantages without jeopardising social and economic stability, of controlling without unduly

delaying the progress of economic change. The following sections will indicate sufficiently the conflicting aims of policy in recent years. It is evident that no resolution of the conflict has as yet been reached, and equally evident that the forces at work are so powerful that the search for a solution must go on.

(ii) . THE GROWTH OF ECONOMIC NATIONALISM.

In the first chapter of this *Survey*, reference was made to some of the ways in which the war of 1914-1918 disturbed economic organisation. It is difficult to measure with any exactitude the extent to which international trade was reduced. The available statistics are complicated by varying degrees of currency inflation, and the movement of war materials is difficult to separate from normal trade, which, indeed, could hardly be said to exist in the abnormal circumstances. Virtually all interchange between the belligerent groups ceased, neutrals were affected by blockades and controls, and, despite the stimulus given to production and trade in areas outside Europe, the bulk of world trade declined heavily.

Apart from the general decline and the very considerable shifts in the relative positions of the various countries in this respect, there were other special factors which rendered commercial policy both complex and unstable at this period. One result of the peace treaties had been the creation of many new States in Europe and considerable alteration of frontiers. In this way, not only were new Customs barriers erected, but new industrial and commercial groupings cut across existing organisation. The revenues needed by States at this period of financial exhaustion reinforced the strong pressure for protection of the new economic units.

The war had left many legacies of trade restrictions and governmental practices which operated as interferences with trade. Requisitions, controls, priority systems, prohibitions of import or export, price fixation, Government monopolies and enterprise all reinforced the effect of tariff barriers. But probably the greatest hindrance to trade arose from the disordered state of the various currencies. Inflation in various degrees, continually changing and increasing taxation, exchange rates that fluctuated not only from day to day but from hour to hour demoralised the contractual basis of regular trade.

It was for this reason that Governments, acting in concert with the international organisation of the League of Nations and through diplomatic conferences, devoted their first efforts at reconstruction to financial and currency problems. The success

of these concerted efforts was encouraging. Agreements, particularly at the Brussels Conference (1920), on the principles of currency and financial administration¹ were quickly followed by efforts to balance national budgets, which ultimately put an end to inflation. Provisional agreement on reparation questions, concerted effort to stabilise the financial situation of certain European countries and a general measure of recovery from the depression of 1921 had restored world production and trade to the pre-war level by 1925 and had also paved the way for further recovery in Europe, which still lagged behind the rest of the world.

The lower level of prices ruling after 1921 had aggravated the effect of tariff barriers by increasing the real burden of the wide ranges of specific duties which had been imposed at a time when prices were higher. The addition of many new tariff barriers, the raising of their levels and the survival of many irritating and restrictive prohibitions and controls imposed during the war also pointed to restrictive commercial policies as an outstanding obstacle to the renewal of international economic co-operation.

The World Economic Conference which met in May 1927 surveyed the whole field of trade restrictions and was practically unanimous regarding the necessity for their removal. The Conference made, in fact, a categorical declaration that "the time has come to put a stop to the growth of Customs tariffs and to reverse the direction of the movement". Three possible lines of action were envisaged — individual action by States with regard to their own tariffs; bilateral action through the conclusion of suitable commercial treaties; and collective action by the negotiation of multilateral agreements. The Conference was important, therefore, mainly as a demonstration of the widespread recognition of the importance of international economic co-operation. Its discussions, resolutions and reports form what is virtually a manifesto of a movement towards freer trade conceived not on national but on international lines. The validity of this general programme has been many times reasserted; but action in such matters is the prerogative of national Governments and, as succeeding events will show, the forces of economic nationalism have overwhelmed them. The course of events has, almost without exception, been away from freer co-operation, so that, in 1932, international trade is, in fact, far more restricted than it was five years earlier when the World Economic Conference unanimously affirmed the value and necessity of freer world trade.

¹ *Report of Brussels Financial Conference, 1920* (document C.10.M.7.1923).

Apart from the survival of many war-time prohibitions, restrictions and hampering regulations, there had been, as soon as the war ended, a remarkable exhibition of nationalist economic policies. In part, they were designed to protect the new industries and channels of trade that had been opened up during the war period. There was fear also of exchange dumping and of renewed competition from Germany. The chemical industries in particular were regarded as vital for military reasons. The heavy industries, like iron and steel, and many so-called key industries were protected also. Great Britain, France and Italy all imposed protective tariffs in the years 1920 and 1921. The newer European States¹ also hastily erected tariff barriers to protect and foster their industrial development. Up till about 1925, therefore, there was a general upward movement of tariffs, particularly marked in relation to industrial products. The memorandum on *Tariff Level Indices*, prepared for the World Economic Conference, shows also that, in many overseas countries such as Australia and India, there had been a marked rise in the tariffs imposed upon manufactured articles.¹

When the World Economic Conference met in 1927, the tariff situation, however, still remained fairly open. With the comparative settlement of currency disorders and the general recovery of production and trade after 1924-25, it was possible, and even necessary in a great many countries, to consider the consolidation and stabilisation of tariff and Customs arrangements that had been devised as temporary measures in the previous years of wide price fluctuations. The whole period 1921-1926 was characterised by great activity in regard to tariff and Customs legislation, and many important commercial treaties and bilateral agreements were concluded. These, however, were mostly for very short periods of a year or less and, in 1927, there still remained the possibility of negotiated concessions and adjustment.

The Economic Consultative Committee set up by the World Economic Conference was able to report at its first meeting in 1928 that "the effect of the Conference has already substantially checked the upward movement of tariffs, which was in full swing in May 1927". The bases for this statement were mainly the abandonment by certain States of tariff increases that had been contemplated, the negotiation of several bilateral agreements which contained tariff reductions, a marked tendency to consolidate and stabilise tariff schedules, and the negotiation of the first multilateral agreement aiming at the abolition of import and export prohibitions and restrictions which had survived

¹ *Tariff Level Indices* (document C.E.1.37). See also A. Loveday, *Britain and World Trade*. London: Longmans, Green & Co., 1931, pages 35-46.

from the war period. An outstanding example of the more co-operative attitude of leading countries was the commercial treaty between France and Germany which was finally agreed upon in August 1927 after negotiations which had extended over three years.

Some progress was being made, therefore, along all three lines which the Conference had laid down — unilateral tariff action, bilateral treaties and multilateral conventions. In addition, a beginning was made with the examination of various forms of administrative protectionism and similar hindrances to the free flow of world trade.

The impetus thus derived from the World Economic Conference was, however, both limited and temporary in its effects. In regard to unilateral tariff action, the most that could be claimed was that, for some months after May 1927, there appeared to be a halt in the imposition of higher duties. The Economic Consultative Committee, in its second report (May 1929), recognised that, while “the check to the forces which are continuously being exerted in every country in favour of greater protection has persisted”, there was, even in 1928, little sign of “a move in the opposite direction”. On the contrary, there were many signs that the protectionist current was setting in more strongly than ever. By the beginning of 1929, there was no longer any doubt of this tendency.

The forces making for higher or lower tariff policies thus seem to have been evenly poised for a few months; but the international outlook faded as the agricultural States of the world began in 1928-29 to feel the first stringency which preceded the depression. In 1928, Persia and China introduced their first autonomous tariffs, while Spain, Peru and Chile made general revisions. In Europe, particularly in Germany and Sweden, there were revisions and eliminations, mostly of a downward character except in regard to the agricultural protection mentioned below. The Economic Consultative Committee at this time recognised that the issue, a drawn battle in 1927-28, would be decided by the character of the new tariffs under consideration in 1929 by Brazil, Egypt, Finland, Mexico, Portugal, Roumania, Spain, Turkey and the United States.

The development of agricultural protection in Europe, however, proved to be decisive. The continuous raising of tariff duties on industrial products in so many States, during the period 1921-1925, had left what the agricultural producers regarded as an invidious and unbalanced tariff situation. As long as food imports were needed in post-war Europe, agricultural prices remained relatively satisfactory; but the new German tariff law of 1925, which reimposed higher duties on food imports,

proved to be the beginning of a strong upward movement of agricultural tariffs designed to protect home agricultural markets. In protecting its agriculturists, Germany had progressively to close its markets to the producers of other countries. In so doing, it became necessary to denounce the commercial treaties with Holland, Finland and Sweden, in so far as they related to imports of agricultural products. Moreover, the original restoration of food duties in 1925 had imposed the "middle rates" of 1902, but successive revisions raised these rates until, in 1929, a new and much more drastic range of duties was imposed, only to be replaced in April 1930 by even more prohibitive rates which, as the depression deepened, were supplemented by the variety of administrative measures discussed later.¹

These developments were paralleled in many other European States, and the agricultural countries of Central and Eastern Europe, crushed between the strong competition from the large-scale cereal and meat producers of the newer lands such as Canada, Australia and the Argentine, and the progressive closing of their neighbouring markets, were themselves forced into high protection and other restrictive measures. As the depression developed, the free markets, particularly for grain, constantly narrowed. Italy, France and Germany erected higher tariff barriers and supplemented them with administrative measures; in Norway, Sweden, Czechoslovakia and Switzerland, State controls or monopolies govern the markets. Milling regulations, quotas, import licences further protect the home growers. In Roumania, on the other hand, there is a direct export bounty, and in Hungary a tax on flour consumption, while in Germany, Poland, France, Czechoslovakia and Austria, the export of cereals is encouraged by the issue of "import bonds" to exporters of grain.

It was this pressure for agricultural protection which destroyed the movement towards freer trade in the years 1927 and 1928. The plight of the agricultural countries of Central and Eastern Europe illustrates very well the fundamental maladjustments that created the depression. The agricultural producers in these countries are faced with heavy competition from overseas exporters, burdened with over-borrowing, their migration restricted, their trade outlets closed. Despite repeated efforts to discover some method of economic co-operation, they are in 1932 forced back, in self-defence, to increasing measures of import restriction, financial difficulties, and lowered standards of living.

¹ See section (iv).

Alarmed at the prospects of a new tariff war, of which the signs were clearly visible in 1929, the meeting of the Assembly in September 1929 had given favourable attention to the proposals made for a "tariff truce" to last for two or three years, during which time negotiations might be undertaken for a more permanent settlement. The immediate effect of the proposed truce was to accelerate action on the part of many States which deemed their tariffs too low, or desired to gain a more advantageous bargaining position. A new impulse was given, therefore, to the already powerful forces making for higher protection. The later development of the proposal for a tariff truce is more conveniently considered below.

From the middle of 1929, the steady deepening of depression, particularly in the raw-material-producing countries, greatly reinforced the pressure for higher tariffs. At this period, there appeared the additional motive of reducing imports in order to provide a strong favourable or active export balance from which the heavy overseas financial commitments of these countries might be met. From this time forward, therefore, the usual protectionist and revenue arguments for higher tariffs were reinforced and quickly overshadowed by the necessity for securing an active "balance of trade".

The whole movement was undoubtedly accentuated both by the alarm and resentment felt in many countries as the discussions of the new Hawley-Smoot tariff dragged on in the United States Congress from May 1929 to June 1930, and by the real effects of that tariff when it went into operation. It was followed quickly by new tariffs in many other countries, among others, Canada, Cuba, Mexico, France, Italy, Spain, Australia, New Zealand. In the case of the British Dominions, higher general tariffs were accompanied by an increased measure of imperial preference, and the general idea of a more extensive system of preferential duties with the British Empire was appreciably advanced.

It is obvious, therefore, that by the end of 1930 the protectionist current was running at full tide. The unilateral action of the various States mentioned above had brought into existence tariffs that were appreciably higher all round. The deepening of the economic depression throughout the year made still more strongly for economic nationalism and, in the scramble for national security, the international aspects of tariff alterations did not weigh heavily.

When the financial crisis supervened in the spring of 1931, the imposition of restrictions upon commerce took on panic proportions. No country was immune, as the difficulty of transferring foreign exchange spread from debtors to creditors.

The rapid succession of tariff changes, exchange controls, contingent systems, clearing arrangements is a confusing story that cannot be treated in detail, but the inevitable results in further restricting the volume of trade, raising the costs and complicating the machinery of trade regulation are only too clear.

Even the briefest record of the details of the almost universal movement towards higher tariffs would be impossible in this *Survey*, but reference should be made to the outstanding case of Great Britain. For more than ninety years, since Sir Robert Peel introduced the budget of 1842, Great Britain had been a free-trade country. Indeed, the movement towards freer trade began much earlier. The length and strength of this free-trade position render its abandonment the more notable. Temporary war restrictions and controls, followed by safeguarding duties for the protection of key industries immediately after the war, had made breaches in the free-trade system; but the reversal of general policy in 1931-32 was more thorough-going and complete. The first step in this reversal of policy was the imposition of temporary duties of 50 per cent on a long list of commodities the importation of which was held to be abnormal in quantity. A further list of agricultural, horticultural and garden imports was met with similar treatment, in this case by the imposition of duties approximating $33\frac{1}{3}$ per cent, but devised, in some cases, on a sliding scale designed to combat the import of early fruit and vegetables. These measures, imposed in November and December 1931, were followed in the early months of 1932 by legislation establishing a wheat quota, and, finally, by a general tariff. The latter was entrusted to a specially constituted permanent committee which in April recommended an extensive list of duties.¹ The range of duties recommended was from 10 per cent to $33\frac{1}{3}$ per cent, the main grouping being at the lower rates. Imports from the British Empire of commodities subject to the new duties are exempt pending negotiations with the Dominions. The commodities covered by the new duties represent a substantial proportion of the total imports of Great Britain. Calculations based upon the trade returns of 1930 show a free list of approximately only a-third of the total imports, while about 40 per cent of the total (excluding 10 per cent, the produce of the Empire) is subject to the new duties. Great Britain, therefore, must now be placed

¹ *Import Duties. Recommendations of the Import Duties Advisory Committee and Additional Import Duties (No. 1) Order, 1932. Cmd. 4066.*

Also "British Tariff Policy 1932" prepared for the Fifth Conference of Institutions for the Scientific Study of International Relations, by Members of a Joint Study Group of the Royal Institute of International Affairs and the London School of Economics and Political Science.

among the countries which have at least a medium-range protective tariff system.

In recommending the first general tariff in April 1932, the Advisory Committee announced its intention not to recommend any lowering of duties for at least a year. Since the tariff as recommended was adopted by Parliament with few major amendments and the power of interim revision is delegated to the Advisory Committee, the use of the tariff for bargaining purposes is somewhat restricted by this pledge. Negotiations are actively under way also with the self-governing Dominions, and an Imperial Conference will meet at Ottawa in July 1932 to discuss the imperial aspects of the new regime. Both in the departure of Great Britain from its free-trade tradition and in the prospect of closer tariff relations within the British Empire, these developments change significantly the whole atmosphere of international discussions on tariffs and trade.

(iii) BILATERAL AND MULTILATERAL NEGOTIATIONS.

If attention is turned to the bilateral treaties which multiplied after 1927, the story is much the same. The method of bilateral negotiation for the reduction of tariff charges was one of the most hopeful avenues of progress envisaged by the World Economic Conference. This was particularly the case when the treaties included clauses for "most-favoured-nation treatment", since successive reductions of duties accrued, not only to the contracting parties, but also to all those countries which had bargained for most-favoured-nation treatment with them.

Numerous treaties were negotiated in 1927 and succeeding years, and it was evident that they held promise, not only of gradual tariff reductions, but also of agreements concerning veterinary controls, Customs formalities and many other measures of administrative protection. The period for which most of them were negotiated was, however, very short, in most cases a year only, and the contracting parties therefore retained liberty of action. As the tide of protectionism rose during the depression, such bilateral agreements became instruments for negotiation on a higher tariff level rather than means for a gradual approach to an all-round reduction of trade restrictions.

As the depression deepened, there were two distinct but related developments of this method of negotiation, particularly among the European countries. There was much discussion of regional agreements, and on December 22nd, 1930, a Convention was signed at Oslo by the representatives of Denmark, Norway, Holland, Sweden and Belgium which

provided a permanent basis for their tariff relations and established a procedure of notification among them in regard to tariff changes.

Other discussions relating to the possibility of regional agreements, particularly among the Central and Eastern European countries, were complicated both by political considerations and by the financial difficulties of those States. Successive conferences of the agricultural countries of Eastern Europe were held at Warsaw (August 1930), Bucharest (October 1930), Belgrade (November 1930) and Warsaw (November 1930). The eight countries represented at these conferences¹ were concerned primarily with the depressed condition of agriculture and particularly of cereal-growing. They contemplated the institution of national controls for the sale and export of these products, but also asked preferential treatment in regard to them from the importing countries of Western Europe. Such preferential treatment, in certain cases, would have cut across the most-favoured-nation clauses of existing treaties, but was strongly advocated as a temporary measure affecting only a comparatively small volume of produce on the ground that agriculture was the fundamental economic basis of the States concerned. This whole discussion was complicated in March 1931 by the announcement of a projected Austro-German Customs Union, a project which was later withdrawn by its proposers.

Bilateral negotiations, extended to the discussion of regional agreements, therefore, led back again directly to the international aspects of trade restriction and regulation. It is convenient at this point to take up the story of the first efforts at multilateral negotiations. The World Economic Conference had recommended this as the third method of approach to freer trade, and in the course of 1928, as has already been stated, a Convention was negotiated for the abolition of import and export prohibitions and restrictions. This Convention was to come into force if eighteen ratifications had been received by September 30th, 1929. At that date, however, only seventeen States had ratified it, and a new conference was called in December 1929 which again failed to secure the necessary agreement.

Another conference held from November 5th to December 5th, 1929, to discuss a Convention giving greater liberty to foreign resident traders, also broke down on the refusal of certain States to change their existing legislation.

The first meeting called to consider concerted economic action in general tariff matters was that convened to take up the proposal advocated at the Assembly in September 1929 for a tariff

¹ Bulgaria, Estonia, Hungary, Lithuania, Poland, Roumania, Czechoslovakia and Yugoslavia.

truce. It met under unfavourable circumstances in February 1930, after the failure of the conferences mentioned above and after it was clear that the new United States tariff would be strongly protectionist. Moreover, the economic depression was now well advanced, and the proposal for a tariff truce was therefore replaced by a commercial Convention of March 24th, 1930, prolonging existing commercial agreements till April 1st, 1931, and setting up a given procedure of consultation to be followed when duties were increased. At the same time, a protocol was signed opening the way to further negotiations of a more permanent character.

It was at this point that the regional discussions in Eastern Europe, and particularly the situation of the Dominion countries, were related once again to the general discussions. The need for financial assistance to these countries was recognised, but strong objections were raised to the granting of preference on cereal products.

The Assembly devoted some attention in 1930 also to this problem. Even stronger objections to the preferential proposals were voiced by the representatives of various non-European agricultural countries. A new turn was given to the whole discussion, however, by the memorandum presented to the Assembly by M. Briand, on behalf of the French Government, proposing the constitution of a Commission of Enquiry for European Union.

Before taking up the account of this Commission's work, however, it is necessary to record the continuation of the efforts to find some basis for concerted economic action in general tariff matters.

A second conference for this purpose met in November 1930 to consider ways and means of putting the Convention of March 24th, 1930, into effect. The Economic Committee of the League had in the meantime considered this problem and suggested the desirability of negotiations for lower tariffs and the consideration of temporary preferential arrangements for the European agricultural countries. The conference, however, remitted the first of these suggestions to the various Governments for bilateral action and, after consideration of the objections raised to the preferential proposals, failed to endorse them. On the other hand, it recommended that an international organisation of agricultural credit should be attempted. No headway was made in regard to the proposed Convention of March 24th, 1930, and, after further discussion at a second session in March 1931, the Convention still remained a project without practical application. The first efforts at multilateral negotiation therefore ended in temporary failure.

Meantime, the Commission of Enquiry for European Union had held a preliminary meeting in January 1931, and had called a meeting at Paris, in the succeeding month, of the cereal exporting and importing countries of Europe, the chief result of which was that the importing countries declared themselves ready to reserve an import quota for wheat produced in Europe and to consider similar action in the case of maize and barley, while deferring for a time consideration of rye and oats. A committee was also set up to consider the problem of disposing of the surplus from future harvests. Later meetings of the Commission of Enquiry were occupied largely with the discussion of a pact of economic non-aggression proposed by the Soviet Union, but the Eastern European countries have maintained their request for preferential treatment of their cereals.

In 1931, however, the whole problem was submerged in the financial difficulties and particularly the controls of foreign exchanges necessitated by the severity of the crisis. Discussions continued both in the Economic Committee of the League and in the Commission of Enquiry for European Union. A draft project for an International Agricultural Credit Association was signed by sixteen States in May 1931, but has not been brought into existence. Various proposals for the alleviation of unemployment and for the facilitating of long-term investments have been mooted. Committees have considered the market situation of special products such as hops, tobacco, etc. But the shadow of the depression has been over all such proposals, financial provision has been wanting, and international economic co-operation has proved impossible, while national Governments have been faced with economic insecurity within their own borders.

(iv) THE CONTROL OF EXCHANGE.

The regulation and restriction of international trade, already gravely complicated by the almost universal raising of tariff barriers and the failure of multilateral negotiations, took on a new aspect in the latter part of 1931, when one debtor country after another was forced to institute drastic controls of the foreign exchanges in order to safeguard the stability of its currency and to provide, as far as possible, the means for meeting its external financial obligations. Exchange controls were unfortunately not altogether a new phenomenon in the post-war world. During the period of currency inflation, the pegging of exchange had been practised by many countries in one way or another. When drastic efforts became necessary to reorganise

and stabilise the currencies which had broken down after severe inflation, these exchange controls were rigidly exercised. With the movement back to the gold standard after 1925, however, the most restrictive of the controls were gradually removed.

Though there were signs of difficulty, for example in Germany, in the summer of 1930, the severe financial phase of the economic depression may be dated from May 1931, when the Creditanstalt difficulties involved the National Bank and the Government of Austria. The weak financial situation that was then revealed, coupled with the effect of the depression upon agricultural prices and therefore upon export values, made it more than ever necessary to provide for larger export balances, while at the same time conserving the exchange parities of the local currencies in order to avoid increasing the burden of external debt, which was already heavily increased by the fall in gold prices. The provision of such an active trade balance might be maximised by encouraging exports or by discouraging imports, or both. The encouragement of exports was a policy that had very definite limits set both by domestic production and consumption and by the capacity and willingness of the international market to absorb increased quantities of the raw materials and food-stuffs, which were the main resources of most of these debtor countries.

Moreover, the protectionist movement had set in so strongly by the middle of 1931 that markets were increasingly restricted. The higher United States tariff of 1930 had been followed by many other tariff systems; both France and Belgium introduced a system of licensing imports in the third quarter of 1931, Czechoslovakia did the same in July, and Sweden introduced a wheat monopoly in June. These and other systems of import controls, it should be remembered, were added to constantly higher tariff barriers, many of them being reprisals against the tariff barriers of other countries. By the end of 1931, licences had led to quota or contingent systems, many countries had left the gold standard, others had thereupon reintroduced additional exchange-dumping duties, commercial treaties were being denounced, and cumulative restrictions were being placed in the way of international trade. A summary list of the main measures adopted will indicate both the universality and the complexity of trade restrictions.

The first type consisted in the control of foreign exchange transactions to check any flight of capital and to conserve the available exchange resources for the most essential national requirements. Such controls were in force in Austria, Bulgaria, Czechoslovakia, Estonia, Finland, Germany, Greece, Hungary, Latvia, Yugoslavia, Argentine, Brazil, Chile and India, while

in Norway the banks exercised unofficial control. During the early months of 1932, Denmark and Roumania introduced control systems, but Finland abandoned such restrictions on December 31st, 1931.

• More direct reduction of imports was achieved in 1931 by the introduction of quotas (Czechoslovakia, France, Italy, Latvia, Netherlands and Turkey); by prohibitions (Czechoslovakia, Denmark, Estonia, Poland, Turkey and Colombia); by State monopolies (Estonia and Sweden); by new import duties (Great Britain); by increased duties (Austria, Argentine, Australia, Belgium, Brazil, Bulgaria, Denmark, France, India, Italy, Latvia, Lithuania, Netherlands, Poland, the Union of South Africa and Switzerland); and by Customs surtaxes for depreciated exchange (Canada and France).

In addition, the abandonment of the gold standard by Argentine, Australia, Brazil, Denmark, Finland, Great Britain, India, Japan, New Zealand, Norway, Portugal and Sweden had considerably hampered imports into those markets. In addition to these countries, Bolivia, Chile, Greece, Siam and Peru abandoned the gold standard in the early months of 1932. In many other countries, its maintenance was more nominal than real, and it was a truer representation of the facts to say that in some half-dozen countries only was the gold standard maintained without special restrictions.

Such a recital of the progressive and cumulative imposition of restrictions in so many countries sufficiently explains the manner in which currency disorganisation in recent months has caused a creeping paralysis of international trade.

There are many other ways, besides the direct effect of higher duties, in which this complication of regulations embarrasses international trade. Formalities have multiplied and become both hampering and costly; licences, if granted for the year, cause gluts and then scarcities, or, if granted monthly, prevent an orderly development of trade. Contingents or quotas cut across most-favoured-nation arrangements and, moreover, dislocate the relations of supply and demand. Decisions taken by civil servants in the "national interest" differ considerably from those dictated by the normal relations of consumer and producer. As a particular important instance of this may be cited the importance attached in the various systems of exchange controls to the service of debt as distinct from the import needs of the country. The world is becoming enmeshed in a network of temporary *ad hoc* regulations which will be extremely difficult to disentangle.

In an effort to cope with certain of these evils, different countries have negotiated bilateral "clearing agreements",

by which imports and exports are balanced as between the two countries concerned. There are, however, very great difficulties, in practice, in maintaining such agreements. International trade is rarely bilateral, and the effort to balance the import and export relations of two particular countries involves the dislocation of the normal many-cornered trade that has been built up by decades of international co-operation. Essentially, such clearing agreements are temporary and unsatisfactory devices to meet an impossible situation.

It is impossible in any brief summary to make anything like a complete statement of all the various devices brought into use to restrict trade. Especially after the abandonment of the gold standard by Great Britain in September 1931, there has been a veritable panic, which has piled new tariffs on old, turned licensing systems into prohibitions, monopolies and contingents; denounced existing commercial agreements; created more and more rigid exchange controls issuing in debt moratoria and paralysed trade; and substituted a slight and temporary framework of clearing agreements for previously existing treaties. The bankers or civil servants have had thrust on them the duty of regulating commercial intercourse, and merchants have been so hemmed in by regulations that freedom of trade has almost ceased to exist.

It would be invidious to take the case of particular countries as anything more than illustrative of general situations. Many of the debtor countries are virtually at a standstill with rigid exchange controls, debt moratoria, and ever-increasing governmental control of economic life. The great creditor countries are almost equally affected. The United States, since its tariff action in 1930, has not added further barriers to trade, but Great Britain, in November and December 1931, placed duties of 50 per cent on three long lists of imports, and followed these lists with two others relating to agricultural imports subjected to duties based on an average of $33\frac{1}{3}$ per cent, besides passing an Act providing for a wheat quota and finally introducing a general tariff.¹ Holland, another traditional free-trade country, raised its tariff barriers in November and, in the following month, introduced a system of "contingents". France and Germany, from the middle of 1931, have striven to protect their agriculture by a very wide contingent system, the imposition of "exchange-dumping" duties and reprisals against other countries which limit either their exports or payment for them.

These are merely examples chosen almost at random. There has never before been such a wholesale and widespread retreat

¹ See section (ii).

from international economic co-operation. The results are already sufficiently manifest in the reduction of trade, which has been outlined in a previous chapter. The full consequences, however, have yet to work themselves out in the standard of living of the peoples of the world. Reversion from a highly organised and interdependent society to the simpler forms of national sufficiency is a costly process, and it has become quite clear that the remedy for international maladjustments is not to be found in a flight to economic nationalism.

(v) THE INTERNATIONAL ASPECTS OF TRADE REGULATION.

Running through this whole story of trade regulation and restriction in the crisis years, there is the definite conflict of economic and social conceptions referred to briefly in the first section of this chapter. In the field of action, national forces and institutions have been completely dominant. The proposals for international action have met with scant success. This is not, after all, difficult to understand. The crisis through which the world has passed, and is still passing, has never been paralleled in duration, universality or intensity. It has brought into challenge the whole of organised economic and political life.

The international conception of developing world unity was by no means widely accepted even before the war. Years of war and post-war struggle and propaganda were hardly likely to establish it, even though the facts of economic development pointed to increasing interdependence. The great bulk of social life and education is still organised on national bases, the preservation of which is regarded as the primary duty of citizenship. There is much that is wholesome and valid in this conception of national life, and it is natural that the advent of a disastrous crisis should evoke a strong impulse to ensure stability in national affairs.

Yet the events of recent years, and more especially of recent months, have demonstrated how large a part international relations have come to play even in national life and affairs. Interdependence, especially in the financial and economic spheres, has been proved, even in the process of endeavouring to secure national sufficiency. The task of synthesis remains. What is valuable and useful for the welfare of the people in national organisation must be reconciled with the fact that every nation is now dependent upon every other.

It is noteworthy, therefore, that, throughout the crisis, international negotiations have been maintained, even in many of the processes of unilateral action. There have been tariff wars

before, never perhaps on such a desperate scale, but, on the other hand, never before conducted internationally. The "habit of conference" has persisted, the multilateral aspect of negotiations has been maintained, even when they have issued in drastic unilateral action. The process may have failed but the machinery is not destroyed.

Moreover, this is the first great economic crisis in which the necessity of international economic co-operation has been steadily maintained, not only as an ideal, but as a practical working solution. Successive official and unofficial conferences have endorsed the recommendations of the World Economic Conference of 1927. Despite national actions to the contrary, even national representatives assembled in international conference have admitted and upheld the validity of this international programme.

There is, therefore, a solid and growing body of support for the view that the way out of the crisis is by an increasing rather than a decreasing measure of international economic co-operation. Action follows upon conviction and conviction waits often upon the exhaustion of other possibilities. Moreover, action in such a vast field cannot be simple. Financial, monetary, commercial and other economic aspects of the problem are interlinked and all depend to some extent upon political settlement and appeasement. The downward slope of the crisis has seen reversion to the more primitive forms of economic nationalism in unprecedented degree; the upward slope awaits and will itself facilitate a return to the realities of interdependence.

Chapter XI.

THE ECONOMIC SITUATION IN JULY 1932.

As the earlier chapters of this *Survey* were being written in the second quarter of 1932, the statistical information available referred mainly to the year 1931 and, in certain cases, to the first quarter of 1932. As the volume goes to press in the middle of July some scattered, and far from complete, statistics are becoming available for the second quarter of the year. It is difficult to draw any very definite conclusions from such fragmentary data ; but they provide the only possible basis for an estimate of the economic position in the middle of 1932.

In such a critical situation as that which exists at the moment of writing, even the comparatively short interval which must elapse between important economic events or movements and the publication of the statistics reflecting their influence is sufficient to render hazardous any estimate of the present position on the basis of past statistics. For example, the diagrams showing movements in exchange rates¹ were prepared just at the moment when substantial changes were imminent in several countries, particularly in Chile and Greece.

It is inevitable that any survey of current events must end *in medias res* ; but the interaction of important political and economic policies which are still in process of formulation renders the present situation and the immediate future more obscure than is usually the case. The agreement reached at the Lausanne Conference on July 9th has only just been announced, the British Imperial Conference at Ottawa has not yet opened its sessions, the Disarmament Conference has not yet formulated the conclusions of its first discussions, and plans are just being launched for an International Economic and Financial Conference later in the year. The London money market is in the midst of the largest debt conversion ever attempted, the balancing of the

¹ Pages 217 and 218.

national budget is occupying the attention of the French and American parliaments, open-market operations by the Federal Reserve Banks are continuing on a large scale, national elections are pending in both Germany and the United States. The decisions reached and the results achieved in such circumstances cannot be known for several months, and it will be some years before their full significance can be appraised.

It is not possible, therefore, to do more at the present time than record the information available concerning economic developments in the second quarter of 1932. This information must be interpreted with much more than the usual qualifications and reserves. Early summer in the northern hemisphere is always a critical time. Harvest prospects are not certain, and there is a heavy seasonal demand for capital with which to finance trade until the harvest receipts become available and also to shift the crops. Financial strain tends to be heaviest at this season ; but in present circumstances, with trade restricted, foreign exchange controlled and capital movements paralysed, the strain is greater than usual. A severe test of endurance is therefore imposed upon those countries which normally borrow at this period in anticipation of the harvest.

Perspective may perhaps best be gained by a comparison of the information available in July 1932, with that upon which a similar estimate of the situation in the summer and early autumn of 1931 was based in a former publication.¹ It is significant that, in 1931, the second quarter of the year proved to be a time of severe financial strain exemplified by the Credit-Anstalt difficulties in May and the Hoover moratorium in June. By September, when the final pages of this former publication were written, the abandonment of the gold standard by a number of important countries had definitely aggravated the financial crisis, but, at the same time, had opened up "possibilities for action on the part of individual nations which may serve to mitigate the depression".²

In the pages which follow, an attempt is made to summarise the position which, in the summer of 1932, had been reached as a result of these conflicting tendencies. In that attempt, however, it is necessary to draw attention to policies of positive action, both national and international, which are in process of development, since these policies will, in the near future, exercise an important influence upon the trend of events. It is not yet possible to do more than draw attention to such important policies as the effort at international political settlement and

¹ *The Course and Phases of the World Economic Depression*, Chapter VIII.

² *Ibid.*, pages 314 and 315.

economic reconstruction begun at Lausanne, the large-scale open-market operations conducted by the Federal Reserve Banks in an effort to expand credit again in the United States, the strong measures taken in many countries to achieve budget equilibrium, the conversion operations in Great Britain, the freer trade initiative launched by the Belgian and Dutch Governments, and the negotiations at Ottawa between the States members of the British Commonwealth. The influence of these policies may perhaps be traced already in certain psychological reactions, particularly of the stock markets ; but their full effect will not be known for some months at least.

In the meantime, the available statistical information is sufficient to indicate that economic activity deteriorated greatly in the second quarter of 1932 and had reached a very low ebb indeed by the end of June. All the statistics that are available support this conclusion as far as the great industrial countries are concerned. There is usually a seasonal increase in production and a decline in unemployment during the early summer ; but in 1932 this improvement in most of the industrial countries was very feeble, while production remained at very low levels.¹ Thus the German index (corrected for seasonal variation) fell to 55.2 per cent of the 1928 level in January and recovered to 57.7 per cent in May ; but this figure compares unfavourably with the 72 per cent reached in May 1931. The Polish index (corrected for seasonal variation) recovered in the same months from 51.8 to 54.6 per cent as against 72.3 per cent in May 1931. In the other countries for which indices are available in these months — Canada, the United States, France, Great Britain, Sweden and Japan — Japan was the only one to show an apparent increase in the early months of 1932, an increase, however, which appears to have been caused largely by the fact that Japan abandoned the gold standard only in December 1931. The improvement which followed the abandonment of the gold standard in the case of Great Britain and Sweden was not fully maintained in the second quarter of the year. There was a similar reaction in Japan also, and an increased curtailment of production in the main industries. The statistics are shown in the following table :

¹ Cf. *Monthly Bulletin of Statistics*, June 1932.

*National Indices of Industrial Production.*¹
(1928 = 100.)

Country	1931	1932				
	May	Jan.	Feb.	March	April	May
Germany (a)	72	55	57	56	54	58
Canada (a)	92	73	74	71	68	
United States (a)	78	65	62	60	58	55
France (b)	102	83	79	77	75	73
Japan	103	97	102	108	104	
Poland (a)	72	52	52	53	55	55
United Kingdom	87 ²	..	..	91 ³	..	..
Sweden (a)	81	85	92	88	85	79

Further evidence of the decline of production may be obtained from the statistics relating to individual industries in various countries. The state of the building industry is often regarded as a significant test of investment activity. The table which follows indicates the depths to which it had fallen in certain countries in the early months of 1932 :

*Indices of Building Activity in Certain Countries.*⁴
(1929 = 100.)

Monthly average	Germany	United States		United Kingdom		France
		Total	Housing	Total	Housing	
1930	74	78	57	101	106	112
1931	40	54	42	84	92	102
1931 : First quarter	35	58	48	89	91	107
Second »	54	68	53	90	98	103
Third »	48	54	37	84	102	100
Fourth »	23	37	29	74	74	100
1932 : First »	12	20	18	76	89	95
April	16	25	18	85	107	88
May	18	30	..	..	..	..

(a) Adjusted for seasonal variations.
 (b) Partly adjusted for seasonal variations.
¹ League of Nations *Monthly Bulletin of Statistics* ; for Germany, *Wochenberichte des Instituts für Konjunkturforschung*, June 29th, 1932.
² Index for the second quarter.
³ Index for the first quarter. The index for the fourth quarter of 1931 was 92.
⁴ *Deutschlands Wirtschaftliche Entwicklung im ersten Halbjahr 1932*, page 14 : Reich-Kredit Gesellschaft, Berlin, 1932.

The most severe contraction of industrial enterprise, however, has been in the heavy industries, and this is most dramatically illustrated by the fact that in the United States the *Iron Age* index of "used capacity" in the steel industry fell, during the week ended July 5th, to 12 per cent.

Against these and similar statistics bearing witness to an unprecedented disorganisation of industrial production, there are certain more cheerful facts to be noted. First, it is evident that those countries which abandoned the gold standard have been more resistant to the continued pressure of deflation. If their production has not greatly recovered, the decline has, in most cases, been stayed. There is some evidence, indeed, that in such countries as Australia a considerable measure of readjustment to lower price-levels has been achieved. Currency depreciation has changed the ratio of prices and production costs in favour of the primary producers, and has restricted imports. Vigorous measures have been taken to reduce costs of production and, at the same time, there has been increased production for export, so that the balance of international payments has become more manageable.

In the countries adhering to the gold standard, also, there is a growing consensus of opinion that readjustments have been taking place; but it is difficult, as yet, to support statements on this point by definite statistical evidence. There appears to be evidence that the prices of producers' goods are less resistant and show more tendency to decline in recent months.¹

It is not possible, however, to place much reliance upon such fragmentary evidence as is now available, especially since the average level of wholesale commodity prices was still falling in the second quarter of 1932. The following table shows the extent of the price decline in various countries:

¹ In Germany, there has been a marked increase in the output of producers' goods, partly for export to the Union of Soviet Socialist Republics. The statistics are summarised in the following table:

*Production of Producers' and Consumers' Goods in Germany.**
(Monthly Average, 1928 = 100.)

	Producers' goods					Consumers' goods				
	January	February	March	April	May	January	February	March	April	May
1929	97	93	102	112	118	97	92	97	101	93
1930	95	91	91	89	85	92	91	91	98	94
1931	66	65	69	70	68	71	76	82	88	84
1932	41	43	45	47	53	74	76	78	74	71

* Source: *Wochenberichte des Instituts für Konjunkturforschung*, June 29th, 1932; *Monatliche Zahlenübersicht C.*

*Index Numbers of Wholesale Prices.*¹
(Average, 1929 = 100.)

Country	Index	1930	1931	1932					
				Jan.	Feb.	Mar.	Apr.	May	June
South Africa . . .	Official	89	86	83	...	...	81	...	...
Germany	"	91	81	73	73	73	72	71	70
Argentina	Banco de la Nacion	96	92	95	95	96	95	94	...
Australia	Official	89	79	78	80	80	79	78	...
Austria	"	90	84	88	86	87	86	89	88
Belgium	"	87	73	65	65	64	63	61	60
Canada	"	91	76	73	72	72	72	71	...
United States . . .	B.L.S.	91	77	71	70	69	69	68	67
France	Official	88	80	70	71	71	70	70	68
India	"	82	68	69	69	67	65	63	...
Dutch East Indies	"	91	71	63	62	62	60	...	...
Italy	Milan	86	71	66	67	66	65	64	62
Japan	Official	82	70	73	73	72	70	68	66
Netherlands	"	82	68	59	58	58	56	56	...
New Zealand	"	97	90	90	89	88	88	87	...
Poland	"	86	74	67	68	67	68	69	65
United Kingdom	Board of Trade	88	76	78	77	77	75	74	...
Sweden	Official	87	79	78	79	78	78	73	77
Switzerland	"	90	78	72	71	70	69	68	67
Czechoslovakia . . .	"	87	79	75	75	74	74	72	...

It is evident that there was, in the second quarter of 1932, a wide range of variation between the levels of prices reached in different countries and between the degree of decline in those countries during 1932. There was a downward tendency in almost every country, even in those which had abandoned the gold standard.

The most recent calculations at the moment of writing indicate some possibility of a check to this downward movement. Bradstreet's weekly index-number of food prices in the United States increased for the last two weeks in June, and the Irving Fisher index-number of wholesale prices rose slightly. The *Economist* index-number in Great Britain also rose slightly in the first fortnight of July. On the other hand, the French, German and Italian index-numbers of wholesale prices were still falling at the end of June.

¹ League of Nations *Monthly Bulletin of Statistics*.

The declining levels of prices and shrinkages of production, which were almost universal in the second quarter of 1932, were accompanied by increased unemployment in France, Germany, Great Britain and the United States of America. The outlook for the northern winter of 1932-33, in default of a marked revival of trade in the autumn, was therefore depressing.

Probably the most striking indication of the paralysis which had overtaken economic organisation is that provided by the statistics of world trade. The latest available figures are summarised in the following table :

Imports and Exports of Forty-five Countries representing approximately 90 per cent of the Value of World Trade.

\$ (000,000's).

Monthly average of first four months.

Country	Imports					Exports				
	1928	1929	1930	1931	1932	1928	1929	1930	1931	1932
Europe. . . .	1,605	1,606	1,479	1,119	767	1,197	1,216	1,168	854	582
North America	436	480	390	245	164	467	544	430	272	174
Rest of World.	498	527	449	287	178	592	598	455	319	224
Total . . .	2,539	2,613	2,318	1,651	1,109	2,256	2,358	2,053	1,445	980

The total shown above indicates that, in the first four months of 1932, the value of international trade was approximately 42 per cent of its value in the first four months of 1929. Moreover, the decline was continuing.

Very important changes were taking place in the distribution of trade also, and in the balances of payments. Perhaps the most striking is the continued shrinkage of exports from the United States, which, in June, resulted in a passive import balance being recorded in the trade of that country. Exports in June were lower in value than in any month since 1914 and in any June since 1904.

A clear illustration of the way in which trade restrictions and regulations are not only reducing the total value of international trade but are altering the direction of such trade as remains may be seen in the quotas of foreign exchange allotted by the Danish Government for imports from Great Britain and Germany respectively. The actual percentages of

imports which entered Denmark from these countries in the first eight months of 1931 are contrasted below with the import quotas allotted for the period June to September 1932¹:

	Actual imports January 1st to September 1st, 1931 Percentage	Quota allotted June 1st to September 1st, 1932 Percentage
Germany	28.0	13.9
Great Britain	13.6	25.2

The balancing of the international accounts becomes increasingly difficult as trade is restricted. Recent statistics show, however, that some measure of readjustment is taking place in certain countries and, in particular, that the balances of commodity trade are becoming increasingly active in the case of most of the debtor countries:

Balances of Commodity Trade.
(First five months of each year.)

Country	Unit	1928	1929	1930	1931	1932
(millions)						
United States . . .	S	+ 213	+ 317	+ 256	+ 81	+ 81
France	Fr.	— 529	— 5,054	— 3,375	— 5,556	— 4,171
Great Britain . . .	£	— 154	— 154	— 155	— 150	— 120
Germany	R.M.	— 1,457	— 578	+ 84	+ 605	+ 460
Australia	£	+ 5	+ 9	+ 10	+ 21	+ 24
New Zealand ² . . .	£	+ 17	+ 15	+ 6	+ 9	+ 11
India	Rupees	+ 361	+ 263	+ 265	+ 81	+ 22
Japan	Yen	— 207	— 266	— 197	— 108	— 264

The list of moratoria on international payments, however, is already a long one,³ and it is clear that international financial payments cannot be fully resumed until there is a much greater measure of freedom of trade than existed in July 1932.

International lending has virtually ceased and, on the contrary, the marked tendency for capital to return to the creditor countries has been accentuated. Since the earlier chapters of this *Survey* were written, the official estimates of the balance of international

¹ *Politiken*, Copenhagen, July 17th, 1932.

² First six months of each year.

³ See Appendix, Table VI. Moratoria, partial or complete, have been imposed on external payments by Peru (June 1931), Chile (July 1931), Uruguay and Brazil (September 1931), Bolivia (October 1931), Salvador (October 1931), Hungary (December 1931), Yugoslavia (April 1932), Greece (May 1932) and Austria (June 1932).

payments of the United States in 1931 has become available. During that year, there was a net inflow of long-term capital to the United States amounting to \$218 million.¹

The German balance of payments for the first half of 1932 also shows clearly the difficulties created by the increased restrictions upon international trade and the stoppage of long-term borrowing.

The table below, adapted from calculations compiled by the Reich-Kredit Gesellschaft,² is not fully comparable with the statements for earlier years published in the preceding chapters of this *Survey*, but is sufficient in itself to show how difficulties have accumulated in the first half of 1932 :

Balance of International Payments in Germany.

(Net balance of inward and outward payments in millions of RM.)

	1929	1930	1931	1932 First six months
<i>Current items (goods, services and gold) :</i>				
Merchandise, including reparation payments in kind	— 44	+ 1,563	+ 2,782	+ 550
Interest and dividends (including amortisation)	— 800	— 1,000	— 1,300	— 700
Other services	— 513	+ 223	+ 152	+ 65
Gold (Reichsbank only)	+ 440	— 67	— 150	— 152
Reparation payments	— 2,501	— 1,699	— 992	—
	— 3,272	— 975	+ 492	— 237
<i>Capital items :</i>				
Long-term debt	+ 229	+ 967	+ 89	— 60
Short-term debt	+ 1,092	+ 32	+ 477	— 45
Other debt	+ 1,071	— 588	— 2,941	
German property released in United States of America	+ 275	+ 377	+ 80	—
Reichsbank Devisen delivery	+ 605	+ 187	+ 1,803	+ 342
	+ 3,272	+ 975	— 492	+ 237

In face of the disquieting situation revealed by such statistics of declining production, falling prices and restricted trade, there

¹ This figure is not comparable with those given for earlier years in other chapters of the *Survey*.

² *Deutschlands Wirtschaftliche Entwicklung im Ersten Halbjahr 1932*: Reich-Kredit Gesellschaft, Berlin, 1932.

is an increasing measure of activity in both national and international efforts to deal with the outstanding obstacles to a resumption of economic activity. The situation in the summer of 1932 differs in this respect from that of a year earlier. National effort varies greatly from country to country. It is convenient to consider the world as now divided into three groups, according to the monetary situation that has developed. The first group consists of countries still adhering to the gold standard without special restrictions; the second, of those countries where nominal gold parity is maintained by restrictions, particularly upon exchange operations; and the third, of those countries which have abandoned the gold standard and have allowed their currencies to depreciate in relation to gold.

These currency difficulties are in themselves a cause of economic deterioration, since they introduce into an already difficult situation the further disturbing element of fluctuating exchange rates reflecting disequilibria between national price-systems. It was largely for this reason that the Gold Delegation of the Financial Committee strongly recommended that a return to the gold standard should be sought "within the shortest possible time".¹ This recommendation has subsequently been endorsed both by the Financial Committee² and by the Bank for International Settlements.³ While, as the Gold Delegation clearly recognised, "the time and level — as well as the particular form of restoration of the gold standard, should that be decided upon — can be determined only by the proper authorities in the countries concerned", and while there are obvious difficulties and dangers in premature and unilateral restoration by particular countries, the value at the present time of an "internationally accepted standard, in order to facilitate the free flow of world trade", is evidently recognised by expert opinion. As long as independent currencies are linked together merely by fluctuating exchange rates, the temptation to seek price advantages in export

¹ Report, *op. cit.*, paragraphs 74 to 83.

² "The Committee has considered during the present session the final report of the Gold Delegation. It believes that this report will prove of real value for those responsible both for monetary and general economic policy, and trusts that special attention will be drawn to it. Further, it desires to state that it is in general agreement with the constructive financial and economic proposals contained in the report of the Gold Delegation." — *Report of the Financial Committee*, July 6th, 1932 (document C.530.M.264.1932 II.A.).

³ Resolution adopted by the Bank for International Settlements, July 11th, 1932: "The Board of the Bank for International Settlements, recognising the necessity of the re-establishment between nations of a monetary system with a common basis, in order to facilitate international settlements under more stable and secure conditions, is unanimously of opinion that the gold standard remains the best available monetary mechanism and the one best suited to make possible the free flow of world trade and of international financing; it is desirable, therefore, to prepare all the necessary measures for the re-establishment of the functioning of the gold standard."

markets by currency manipulation is very strong ; but an international competition in that direction might become an extremely dangerous threat to the continuance of such international trade as remains.

The economic situation of those countries which are maintaining nominal gold parity by means of restrictions upon trade and financial payments is necessarily weak. In many of them, complete or partial moratoria and standstill agreements have temporarily relieved the strain upon their resources for external payments. Increasing restrictions upon their international trade place a considerable strain upon their price-levels, and it is generally recognised that, even with outside help such as the international loan projected for Austria,¹ their recovery awaits more far-reaching measures of reconstruction, and particularly an improvement in the general world situation.

The position of the countries which have abandoned the gold standard is, in most cases, dominated by the developments in Great Britain. This is particularly true of the so-called "sterling group", which have managed their currencies so as to maintain a stable rate of exchange with sterling. Some of these countries, notably Australia and New Zealand, have embarked upon extended policies of cost reduction by such means as the reduction of wages, interest rates and rents. All of them have gained in so far as Great Britain offers a market for their produce, and it is significant that this gain was held to outweigh the possible advantage they might have derived in respect of their financial obligations to Great Britain if their currencies had been maintained at gold parity.

In Great Britain itself, the immediate effect of the abandonment of the gold standard was a stimulus to production and exports as well as to security prices. Continued deflation in the gold standard countries prevented that stimulus from developing very far ; but the domestic situation was relieved. Other measures, such as the balancing of the budget, contributed to a strengthening of public confidence; and a return of capital, added to a reduction of imports, strengthened the position of Great Britain on international account. In March and April, there was a distinct upward pressure on sterling exchange and some indication of a movement of short-term speculative funds to the London money market. The Bank of England was enabled to buy gold — in itself an indication that the balance of payments was becoming more favourable — and the discount rate was lowered successively, till it reached 2 per cent on June 30th, 1932.

¹ League of Nation Austrian Protocol (document C.539.M.270.1932.II.A.) Geneva, July 15th, 1932.

On that date, the Chancellor of the Exchequer announced the scheme by which £2,000 million of War Loan bearing 5 per cent interest was to be converted to a 3½ per cent basis. At the moment of writing, in the middle of July, the conversion operations are not completed, but there are indications that they will be successful. The economy (estimated at a net figure of £23 million) in public expenditure will not be realised until 1933, but the more immediate effects of the scheme are already important. Security prices have risen substantially, rates of interest tend to be reduced, and there is a stronger feeling of confidence in the immediate future.

The effect of the low discount rate upon commercial enterprise cannot yet be estimated. There is a somewhat weaker tendency in the sterling exchange; but, by an arrangement between the Treasury and the Issuing Houses, new issues are not being floated while the conversion operations are being completed. It is not yet possible to estimate what the effect of the conversion will be upon domestic rates of interest, domestic price-levels, the external value of sterling, and the prospects of a resumption of foreign and dominion lending. Even if it were possible to sketch a theoretical sequence of probabilities arising from this single cause, it is not possible to foresee the course of prices and other important developments in other countries.

In the countries which still adhere without special restrictions to the gold standard, there has, in recent months, with one important exception, been a continuous deflation of the price-level and an effort to achieve a new equilibrium on the basis of lower costs of production. This tendency is clearest in Belgium and Holland, but is marked also in France, Poland, Switzerland and Italy. The level of wholesale prices has also fallen steadily in the United States, but, at the end of February, the Federal Reserve Banks began open-market operations on a large scale with the avowed object of arresting the fall in the price-level in so far as it was caused by credit restriction. These operations have been used to supplement other efforts at reconstruction by monetary policy, and it is necessary at this point to review briefly the measures that have so far been taken in this direction.

When the liquidity crisis, together with the "gold rush" on New York, developed shortly after the widespread abandonment of the gold standard in September and October 1931, there was a considerable impetus to deflation in the United States. A severe financial stringency was created and bank failures rose to an alarming degree. In the last three months of 1931, gold to the value of \$191 million left the United States, as a result mainly of European short-term balances and earmarked gold being withdrawn.

The first effort made to stem the banking panic that ensued was the formation, on October 7th, of the National Credit Corporation, an organisation of commercial banks designed to mobilise credit in order to assist the weaker banks. The proposed capital of \$500 million was not subscribed and total advances did not much exceed \$10 million. When the Reconstruction Finance Corporation was formed on December 8th, it took over these advances.

The Reconstruction Finance Corporation, modelled on the War Finance Corporation, is a governmental institution with capital subscribed by the United States Treasury, but with the right to issue bonds and notes to an amount equal to three times the subscribed capital. Its purpose is to make "amply secured" advances, for periods up to three years, to banks and other institutions. It has functioned, therefore, as an instrument by which financial difficulties have been averted, or temporarily remedied. Its purpose has been to salvage embarrassed financial institutions and, in that way, to stay the panic. It is not an instrument for credit expansion leading to rising prices and recovery.

After a good deal of debate and controversy, however, legislation was also passed with the object of enabling the Federal Reserve Banks to undertake credit expansion on a more considerable scale. The principal provisions of the Glass-Steagall bill, which became law on February 27th, 1932, concerned the conditions under which the Federal Reserve Banks were empowered to substitute "eligible paper" for gold in the statutory reserves maintained against note issues and other sight liabilities. The object of the legislation, in simple terms, was to allow the Federal Reserve Banks to use Government securities as well as approved commercial bills as "eligible paper", and therefore to give them the possibility of sustaining and expanding credit without making great inroads upon the limited supply of commercial bills, while, at the same time, freeing a proportion of the gold reserves to meet external drains.

The passing of this legislation made it possible for the Federal Reserve Banks to undertake open-market operations on a large scale by purchasing Government securities. If, under the former legislation, such operations had been attempted at a time when there was a large and sustained demand for gold for export, the purchases of commercial bills that would have been necessary would have impaired the liquidity of the commercial banks by weakening their bill portfolios.

The new legislation, allowing the Federal Reserve Banks to use their extensive purchases of Government securities as cover for a certain proportion of the notes issued, put them in possession of larger amounts of "free gold"—*i.e.*, gold over and above that

necessary for reserve purposes. This increase in the amount of "free gold" enabled them fully and promptly to meet a foreign demand which amounted to \$420 million in the first five months of 1932.

At the same time, the large open-market operations which were undertaken contributed materially to easing the strain upon the banking system. In the following table, the significant statistics which illustrate the effect of the credit expansion are stated summarily :

Movements of Federal Reserve Credit 1932. ¹
(000,000's omitted.)

Date	Government securities	Bills discounted	Reserve balances of member banks	Monetary gold stock		Money in circulation	
				Total	Federal Reserve Banks	Total	Federal Reserve notes
End of :							
January . .	746	899	1,947	4,415	2,976	5,642	2,648
February . .	740	828	1,849	4,353	2,938	5,603	2,634
March . . .	872	639	1,924	4,390	3,020	5,459	2,546
April . . .	1,228	556	2,124	4,367	3,004	5,464	2,551
May	1,549	490	2,113	4,150	2,790	5,479	2,558
June 9 . .	1,645	502	2,112	3,839	2,627	5,452	2,557
» 16 . .	1,692	496	2,101	3,909	2,561	5,467	2,576
» 23 . .	1,730	488	2,066	3,917	2,563	5,505	2,616
» 30 . .	1,801	470	2,034	3,920	2,579	5,649	2,756
July 7 . .	1,801	500	1,963	3,922	2,578	5,775	2,868
» 14 . .	1,821	516	2,015	3,932	2,588	5,714	2,836
» 21 . .	1,836	538	2,036	...	2,609	...	2,862
» 28 . .	1,841	525	2,072	...	2,621	...	2,834

In considering this table, attention should be directed first to the very substantial increase in the holdings of Government securities. This increase, the result of open-market operations, is reflected in movements of the other series. It has partly achieved its purposes of reducing the indebtedness and increasing the credit balances of the member banks with the Federal Reserve Banks. The position, in these respects, is set out in the columns showing the amounts of bills discounted and of balances held.

¹ Sources : Monthly figures, see *Federal Reserve Bulletin* ; weekly figures, see *Commercial and Financial Chronicle* and *The Economist*.

There was some tendency to improvement until a recrudescence of banking failures, particularly in Chicago in June, caused renewed apprehension of widespread runs and led member banks once again to improve their position in respect of liquidity by again rediscounting with the Federal Reserve Banks.

Part of the increased credit made available by the open-market operations has, however, been neutralised, first, by the heavy losses of gold for export and, secondly, by an apparent renewal of domestic hoarding of notes. The tendency in recent weeks for these "factors of decrease" to cause a shrinkage in the volume of central bank credit available to the American banking system is shown clearly in the last two columns of the preceding table.

The extent to which the attempted credit expansion by the Federal Reserve Banks has, in fact, relieved the member banks and exercised through them an influence upon industry is very difficult to measure at the present time. Bankruptcies decreased greatly, both in number and amount, and an increasing number of banks were being re-opened until the failures in Chicago again renewed the strain. Central bank credit expansion penetrates to industry only slowly and by devious channels. The first essential result is to relieve the position of the commercial banks. If their indebtedness is reduced and their balances increase, an expansion of commercial credit many times greater than the amount of central bank credit made available to them can ensue and quickly spread from one industry to another. It is as difficult to catch the exact moment when continued central bank credit expansion begins to take effect as it is to be sure of the turn of the tide in a shallow, open bay. Before the renewed banking failures in June, there was some indication that the forced liquidation of securities was slackening, and the total of loans and investments of reporting member banks in leading cities increased slightly in May for the first time in many months. The fact that they fell again in June reflected a renewal of banking strain. Bank deposits were increasing also, and it was known that foreign short-term balances had been reduced to minimum amounts, so that large-scale gold exports were likely to cease, at any rate for a time. Despite the break in confidence occasioned by the more recent banking failures, it was felt that the way was more open for continued open-market operations to become effective in a substantial increase of actual commercial investments.

From the preceding brief summary of some of the outstanding efforts being made to check the depression and restore equilibrium in the economic organisation of different countries, it will be clear that there is no generally accepted agreement upon the

measures necessary for recovery. As was suggested in an earlier chapter,¹ the lack of international agreement, particularly upon monetary policy in relation to price-movements, leads to national efforts at readjustment along inflationary or deflationary lines which would be irreconcilable if the abandonment of the gold standard had not substituted fluctuating foreign exchanges for fixed gold parities in many countries. The position of the United States *vis-à-vis* the other countries which remain on the gold standard is the outstanding exception in this respect. The recent banking legislation of the United States has been reviewed in the preceding pages, together with such information as is available concerning the actual banking situation. Particular attention has been paid to the effort being made to arrest the depression in that country, not only because of the great importance of the American situation in itself, but also because of its probable effect upon economic developments in the world as a whole. The success of a continued resolute policy of credit expansion, even though it involved further drains on the gold reserves, would make for a revival of speculative, and therefore industrial, activity in the United States, and would bring the possibility of credit expansion based upon increasing gold reserves in the other gold-standard countries; but such success is obviously dependent upon a restoration of business confidence in the United States and upon the banking policies pursued in the other gold-standard countries. It is too soon yet to judge whether the measures so far taken will prove adequate in the long run to bring about credit expansion in sufficient volume to cause an upward movement of prices. If this should prove to be the case, or if the expansionist policy is pursued further until it does bring about a rise in the American price-level, it is obvious that this will not only facilitate the accumulation of gold reserves in other countries, unless in the meantime they also expand credit *pari passu* with the United States, but will also enable those countries that have abandoned the gold standard to pursue cheap credit policies without running an undue risk of their foreign exchange declining.

In the sphere of international action, positive progress in economic and financial matters has yet to be achieved. The Lausanne Conference did not approach such matters directly. In so far as the agreement reached at that Conference removed one of the stumbling-blocks to recovery and took some steps towards political *rapprochement*, it facilitated future consideration of economic and financial action. The agreement to substitute one final obligation at some future date of three milliard RM.

¹ Chapter IV, section (iv).

(\$600 million) for the German reparation obligations under the Young Plan is conditional upon ratification by the Governments concerned. The problem of war debts remains to be considered, and, pending its settlement and ratification of the reparation agreement, the positive economic, as distinct from political, results of the Lausanne meetings are practically equivalent to an extension of the Hoover moratorium upon reparation and debt payments, at least until the next debt payments to the United States fall due on December 15th, 1932. The larger results of the conference lie in its psychological effects, and these cannot as yet be accurately estimated.

The economic consequences of other recent international discussions must also await consideration in succeeding issues of this *Survey*. Mention should be made of the League Protocol for further financial aid to Austria which, at the moment of writing, has been signed but not yet ratified; the impending discussions of the British Imperial Conference at Ottawa; the projected International Economic and Financial Conference; and the Customs Agreement recently signed by the representatives of Belgium, Luxemburg and the Netherlands.

Of these, the latter only is as yet a reality. On June 20th, at Lausanne, the representatives of the three States concerned initialled an international Convention for the reduction of restrictions upon international trade between their countries. The Convention was definitely signed at Geneva on July 16th. The main clause of the Convention provides for an immediate reduction of 10 per cent of existing Customs duties upon imports from the countries concerned, and further reductions of an equal amount each year, up to 50 per cent in the fifth year, provided that duties shall not be reduced below a minimum of 4 per cent *ad valorem* on semi-manufactured products and 8 per cent on wholly manufactured products.¹ New measures of prohibition, restriction or regulation of imports will not be undertaken save in exceptional circumstances, in which cases quotas shall be fixed at 100 per cent of the average quantities imported or exported in normal years. Existing prohibitions and restrictions will be abolished as soon as possible.

The importance of this Convention, which comes into force fifteen days after the deposit of the second ratification, lies not only in the fact that it is the first definite and practical move towards freer trade since the depression, and, indeed, for some years before that. An essential feature of the agreement is that it is open to the adhesion of all States on a footing of complete

¹ The limit below which duties on agricultural goods shall not be reduced has not yet been settled.

equality. Unlimited and unconditional most-favoured-nation treatment is to apply to all the contracting parties. It is clear, therefore, that the Belgo-Dutch initiative may possibly be developed into a collective treaty for the reduction of tariff duties and the removal of other trade restrictions as recommended by the Economic Committee of the League in pursuance of discussions at the World Economic Conference of 1927.

While the provisions of the treaty include an obligation not to raise duties against other States to which the contracting parties are bound by commercial Conventions, the right is reserved to impose further duties if such States further increase their duties or impose more restrictions on trade. There is, therefore, a possibility of a preferential regime developing in favour of those States which adhere to the Convention. Moreover, it is possible that the Convention may involve some modification of existing most-favoured-nation clauses in existing treaties with States which do not adhere to the Convention.

While an important lead has been given in the direction of freer trade, it is not yet certain how far this initiative will be successful. In the meantime, outside Belgium, Luxemburg and the Netherlands, no progress has been made in the removal either of tariffs or of exchange controls and similar restrictions upon international trade. On the contrary, these continue to multiply, and the strangling of international trade which results becomes a greater and greater obstacle to economic recovery.

This *Survey* closes, therefore, at a time when important steps towards political settlement and economic reconstruction have been taken and others are in preparation. It is too soon to appraise the results that have so far been achieved; but a note of cautious optimism is sounded by the first reactions of the stock exchanges. Relief is perhaps a better word than optimism. It is hoped that further disaster may have been averted; but the problems still awaiting solution are many and difficult. Even when business enterprise is freed from the political and psychological burdens that have weighed heavily upon it, the reconstruction of economic activity will still entail laborious and continued effort.

STATISTICAL APPENDIX

Table I.

CHANGES IN THE QUANTUM OF TRADE BY CLASSES OF COMMODITIES. ¹
(Base : 1913 = 100.)

France.

Year	Area	Prices	Imports				Exports			
			Food	Raw Materials	Manu- factures	Total	Food	Raw Materials	Manu- factures	Total
1913	Pre-War		100	100	100	100	100	100	100	100
1919	Post-War	1913	162	74	216	121	42	30	53	45
1920			127	82	200	114	80	59	100	86
1921			99	68	103	82	76	65	94	83
1922			118	98	127	108	66	78	95	86
1923			124	103	108	109	92	83	114	103
1924	Saar incl.	1924	130	112	108	115	108	89	135	119
1925			113	107	94	106	91	99	142	124
1926			113	114	100	111	97	101	156	134
1927			130	112	76	109	96	121	167	146
1928			119	119	105	116	116	120	168	148
1929	Pre- ceding years		131	130	143	133	111	116	169	147
1930			137	134	179	143	114	108	145	131
1931			181	118	165	141	89	95	124	112

Percentage distribution by classes of total imports and total exports :

1913			21.6	58.7	19.7	100	12.2	27.0	60.8	100
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Germany.

Year	Area	Prices	Imports				Exports ²			
			Food ³	Raw Materials	Manu- factures	Total ⁴	Food ³	Raw Materials	Manu- factures	Total ⁴
1913	Pre-War		100	100	100	100	100	100	100	100
1922	Post- War, excl. Saar	1913				59				61
1923						45				53
1924			75	55	81	63	33	35	59	51
1925			97	76	101	84	38	64	70	65
1926			94	67	73	74	41	89	76	75
1927	Pre- ceding years		112	100	139	107	35	84	84	79
1928			108	98	134	104	52	90	94	89
1929			101	97	123	100	67	100	106	101
1930			92	88	103	90	56	93	102	98
1931			78	76	81	76	55	72	93	89

Percentage distribution by classes of total imports and total exports :

1913			26.1	58.3	12.9	100	10.6	22.5	66.8	100
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¹ All figures relate to special trade. Classification differs from country to country and comparison between countries is therefore invalid.

² Reparation payments in kind included.

³ Living animals excluded.

⁴ Living animals included.

Table I (concluded).

CHANGES IN THE QUANTUM OF TRADE BY CLASSES OF COMMODITIES.

(Base : 1913 = 100.)

United Kingdom.

Year	Area	Prices	Imports				Exports			
			Food	Raw Materials	Manu- factures	Total ¹	Food	Raw Materials	Manu- factures	Total ¹
1913			100	100	100	100	100	100	100	100
1920	British Isles	1913	86	95	84	88	55	48	77	71
1921			91	62	60	74	49	45	51	50
1922			99	79	75	86	53	95	67	69
1923	Great Britain and Northern Ireland	1924	115	79	90	97	69	107	73	77
1924			125	90	105	109	86	89	79	80
1925			123	96	118	113	83	80	80	79
1926			122	107	125	119	81	49	74	71
1927			128	102	135	121	86	82	82	82
1928			127	91	136	118	91	80	85	84
1929			131	102	142	124	103	91	86	85
1930		1930	132	91	142	121	96	75	69	70
1931			144	86	145	124	80	61	50	73

Percentage distribution by classes of total imports and total exports:

1913			42.3	31.3	26.0	100	6.5	12.6	78.8	100
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¹ Including living animals (not for food) and parcel post.

Sources :

France : *Indices généraux de mouvement économique de la France*, page 117 ; *Bulletin de la Statistique générale de la France*.

Germany : *Monatliche Nachweise über den auswärtigen Handel Deutschlands* ; *Statistisches Jahrbuch für das Deutsche Reich*, 1926-1931.

Great Britain : *Board of Trade Journal*, 1925-1931. Bureau of Foreign and Domestic Commerce : *United Kingdom*. Washington, 1931.

Table II.

INDEX OF WORLD PRODUCTION OF FOODSTUFFS AND RAW MATERIALS,
1881-85 to 1909-13 (A):

Commodity	Quantum of Production			c Price in \$ per unit	Value of Production at 1913 Prices (\$) 9	
	Unit (000,000's)	a 1881-85 Yearly average	b 1909-13 Yearly average		d 1881-85 Yearly average	e 1909-13 Yearly average
1. Wheat	quintals	642	1,067	3.32	2,131	3,542
2. Rye	quintals	342	452	3.88	1,327	1,754
3. Barley	quintals	224	402	2.11	473	848
4. Oats	quintals	375	678	2.59	971	1,704
5. Maize	quintals	582	1,067	2.53	1,472	2,699
6. Coffee	quintals	6.0	11.2	21.45	129	240
7. Cocoa	quintals	0.5	2.4	28.70	14	69
8. Tea	quintals	1.6	3.8	36.42	58	138
9. Tobacco	quintals	7.9	13.0	28.22	223	367
10. Foodstuffs	quintals				6,798	11,361
11. Cotton	quintals	18.5	48.1	28.00	518	1,347
12. Wool	quintals	8.0	13.4	43.35	347	581
13. Silk	quintals	0.093	0.256	7,466	69	191
14. Pig-iron	metric tons	14.8	17.2	14.45	214	249
15. Steel	metric tons	5.98	65.2	25.38	152	1,655
16. Silver *	kg.	3.06	7.01	19.23	59	135
17. Copper *	metric tons	0.23	0.97	336.62	67	327
18. Tin *	metric tons	0.046	0.133	939.55	42	125
19. Zinc *	metric tons	0.29	0.98	126.34	37	124
20. Lead *	metric tons	0.45	1.16	93.49	42	108
21. Aluminium *	metric tons	0.00001	0.064	521.2	0	33
22. Nickel *	metric tons	0.0015	0.310	837.76	1	26
23. Coal and lignite	metric tons	397	1,212	2.43	965	2,945
24. Petrol	metric tons	4.58	45.90	6.72	31	308
25. Rubber *	metric tons	0.015	0.125	1,349.5	20	169
26. Potash	metric tons	1.04	9.62	23.82	25	229
27. Raw materials					2,589	8,552
28. Total foodstuffs and raw materials					9,389	19,913

* Production in 1885 and 1913.

(A) Sources of Estimates:

¹ Sundbärg: *Aperçus statistiques Internationaux*, Stockholm, 1908.

² Statistique générale de la France: *Annuaire statistique*, Paris, 1931.

³ Estimated on the basis of incomplete figures of national production supplemented by trade statistics; see also *l'Annuaire statistique français* and Page: *Commerce and Industry*, London, 1919, Statistical Tables.

⁴ Sundbärg gives 20,700,000 tons for 1881-85. As all steel at that time was made from pig-iron, 5,900,000 tons, the average steel production in that year, has been deducted in order to arrive at the production of pig-iron exclusive of that used for steel production.

⁵ International Institute of Agriculture *Year-Book*; see also League of Nations *International Statistical Year-Book*, 1928.

⁶ League of Nations *International Statistical Year-Book*, 1928.

⁷ Statistique générale de la France: *Annuaire statistique*.

⁸ It is estimated that 75 per cent of the world pig-iron production in 1909-13 was used for steel production.

⁹ Prices used for calculating the League of Nations' Index of World Production of Foodstuffs and Raw Materials.

Table III.

NOTES IN CIRCULATION, 1929 TO 1932.

(000,000's)

Country	Notes	Currency	End of			May 1931	May 1932
			1929	1930	1931		
Albania	Bank	Franc	11.5	12.9	11.9	12.7	
Argentina	State	Peso	1,247	1,261	1,246	1,252	
Australia	Bank	£	45.3	48.2	54.8	50.7	
Austria	»	Schilling	1,094	1,090	1,183	1,141	995
Belgium	»	Franc	13,933	16,419	18,270	16,092	18,040
United Kingdom	»	£	370	369	364	355	354
Bulgaria	»	Lev	3,609	3,296	2,919	3,183	2,675
Canada	Bank and Dominion	\$	188	163	159	157	
Chile	Bank	Peso	352	306	319	293	
Czechoslovakia	»	Koruna	8,230	7,824	7,679	6,732	6,582
Danzig	»	Gulden	37.8	37.9	44	35.1	
Denmark	»	Krone	367	360	346	342	318
Estonia	»	Ekr.	34	32.2	35.2	32.9	32.2
Finland	»	Markka	1,361	1,279	1,293	1,257	1,168
France	»	Franc	68,571	76,436	85,725	78,185	81,418
Germany	Reichsbank	R.M.	5,044	4,778	4,776	4,299	3,961
Greece	Bank	Drachma	5,193	4,803	4,003	4,304	4,060

Hungary	Bank	Pengō	501	469	423	370	370
India	State	Rupee	1,794	1,613	1,793	1,548	1,685
Irish Free State	Currency Commission	£	14.2	14.3	13.4	13.7	
Italy	Bank	Lira	16,774	15,680	14,295	14,722	
Japan	"	Yen	1,642	1,436	1,331	1,078	
Latvia	State and Bank	Lat	83	87	76	75	
Lithuania	Bank	Litas	95	117	109	109	96
Netherlands	"	Gulden	851	843	1,023	837	1,006
New Zealand	"	£	7.2	6.7	7.3	5.6	
Norway	"	Krone	318	312	334	291	304
Poland	"	Zloty	1,340	1,328	1,218	1,222	1,103
Roumania	"	Leu	21,144	19,605	23,750	18,709	21,982
Spain	"	Peseta	4,433	4,724	4,949	5,197	4,830
Sweden	"	Krona	569	594	583	542	553
Switzerland	"	Franc	999	1,062	1,609	990	1,535
Union of South Africa	"	£	7.5	7.1	7.3	7	
United States	"	\$	2,463	2,267	3,263	2,224	
U.S.S.R.	State	\$	266	297	289	301	
Yugoslavia	Bank	Rouble	1,501	2,080	2,734 ¹	2,181	2,767 ¹
	"	Dinar	5,818	5,397	5,172	4,791	4,942

¹ Gross issue.

Table IV.

SITUATION OF THE STATE DEBT OF VARIOUS COUNTRIES AT THE END OF THE FINANCIAL YEAR 1930 (1930-31), OR NEAREST AVAILABLE DATE, EXPRESSED IN U.S.A. DOLLARS (000,000's).

Country	Date	Total Debt	Total Foreign Debt	Domestic Debt		Foreign Debt	
				Funded	Floating	Funded	Floating
Austria	31. XII. 1930	294.8	275.5	19.3	—	275.5	—
Belgium	31. XII. 1930	7,326.0	3,733.9	3,592.0	0.1	3,733.9	—
Bulgaria ¹	31. III. 1931	167.8	123.3	40.3	4.2	122.7	0.6
Czechoslovakia	31. XII. 1930	988.6	188.0	707.9	92.7	126.6	61.3 ²
Estonia	31. III. 1931	0.35	0.3	(0.001)	(0.03)	—	—
Finland	31. XII. 1930	95.7	85.4	10.3	—	80.9	4.5
France	31. III. 1931	18,872.2	7,762.9	9,575.1	1,534.2	—	—
Germany ³	31. III. 1931	2,883.4	788.4	1,746.5	348.5	663.2	125.2
Greece	31. III. 1931	535.0	405.0	76.3	53.7	389.8	15.2
Hungary ³	31. XII. 1931	310.9	272.5	23.1	15.3	219.1	53.4
Italy ⁴	30. VI. 1931	4,871.7	90.9	4,501.2	279.6	90.9	—
Netherlands	31. XII. 1930	1,091.7	—	959.9	131.8	—	—
Poland	31. XII. 1930	494.8	447.6	47.2	(0.01)	—	—
Portugal							
Roumania	31. XII. 1930	1,104.5	1,005.6	94.8	4.1	—	—
Spain	31. XII. 1928	3,159.3	152.3	2,966.3	40.7	152.3	—
United Kingdom of Great Britain and Northern Ireland	31. III. 1931	36,868.8	5,186.4	28,792.9	2,889.5	5,186.4	—
Yugoslavia	1. VII. 1930	741.2	—	—	—	—	—
Australia	30. VI. 1930	5,048.3	2,631.0	2,387.5	29.8	2,608.1	22.9
Canada	31. III. 1931	2,606.1	518.6	1,797.4	290.1	518.6	—
United States of America	30. VI. 1931	16,801.5	—	13,530.5	3,271.0	—	—

¹ Bulgaria. — Excluding (a) reparation and occupation debt; (b) compensation for property of Bulgarian nationals, sequestered and liquidated in England; (c) indemnities due to European Danube Commission; (d) Bulgaria's share in Ottoman public debt; (e) debt to Russia in respect of occupation of former Eastern Roumelia.

² Czechoslovakia. — The floating foreign debt is practically funded under agreements, in accordance with which payments are being made, but which are not yet ratified by Czechoslovakia.

³ Germany, Hungary. — Excluding reparation debt.

⁴ Italy. — Excluding war debt to the United Kingdom and the United States of America, counterbalanced by reparation receipts.

Table V.

STATE DEBT SERVICE, POPULATION AND TRADE OF VARIOUS COUNTRIES DURING THE FINANCIAL YEAR 1930 (1930-31), EXPRESSED IN U.S.A. DOLLARS (000,000's).

Country	Population : C. Census or E. Estimate, XII. 1930 (000,000's)	Financial Year : Accounts	Service of :						Trade (special) by value (000,000's)		
			Total Debt	Foreign Funded Debt			Foreign Floating Debt	Total Foreign Debt	Imports	Exports	Balance
				Total	Inter- est	Amort- isation	Interest				
Austria	6.7 C.	1930 Cl. Accts.	23.1	21.3	13.6	7.7	—	21.3	380	260	— 80
Belgium	8.1 C.	1930 Estimates	413.8 ¹	.	.	(215.0) ²	.	.	860	730	— 130
Bulgaria	5.9 E.	1930-31 Estimates	9.0 ³	6.0	5.5	0.5	—	6.0	33	45	+ 15
Czechoslovakia	14.7 E.	1930 Cl. Accts.	72.1	16.7	13.6	3.1	—	16.7	464	517	+ 53
Estonia	1.1 E.	1930-31 Cl. Accts.	(5.6 Kr. = \$0.01)	.	.	.	.	(5.2 Kr. = \$0.01)	26	26	...
Finland	3.4 E.	1930 Cl. Accts.	7.1	6.1	4.5	1.6	0.4	6.5	132	136	+ 4
France	41.8 E.	1930-31 Estimates	517.9 ¹	.	.	.	.	.	2,052	1,679	— 373
Germany	64.5 E. ⁴	1930-31 Cl. Accts.	273.9 ⁵	.	.	.	.	.	2,476	2,867 ⁶	+ 391
Greece	6.4 C.	1930-31 Estimates	46.1	23.3	17.3	6.0	(0.01)	23.3	141	74	— 67
Hungary	8.7 C.	1930-31 Estimates	15.1 ⁷	14.0	10.4	3.6	.	.	146	159	+ 13
Italy	41.1 E.	1930-31 Cl. Accts.	495.7 ⁸	42.5	.	.	—	42.5	911	637	— 274

¹ Belgium, France. — Budgetary charges only, not including those met out of amortisation fund.² Belgium. — Includes amortisation effected by both the budget and the amortisation fund.³ Bulgaria. — Excluding reparation payments, amounting to \$1.9 million, and other war charges, \$0.4 million.⁴ Germany. — Population excluding that of Saar Territory.⁵ Germany. — Excluding reparation payments, amounting to \$395.4 million, and other war charges, \$1.2 million.⁶ Germany. — Exports include war reparation payments in kind amounting to \$168 million.⁷ Hungary. — Excluding reparation payments amounting to \$1.5 million.⁸ Italy. — Includes charges met out of various amortisation funds.

Table V (concluded).
STATE DEBT SERVICE, POPULATION AND TRADE OF VARIOUS COUNTRIES DURING THE FINANCIAL YEAR 1930
(1930-31), EXPRESSED IN U.S.A. DOLLARS (000,000's).

Country	Popu- lation : C. Census or E. Estimate, XII, 1930 (000,000's)	Financial Year : Accounts	Service of :						Trade (special) by value (000,000's)		
			Total Debt	Foreign Funded Debt			Foreign Floating Debt	Total Foreign Debt	Imports	Exports	Balance
				Total	Inter- est	Amorti- sation						Interest
Netherlands . . .	7.9 E.	1930	74.1	—	—	—	—	—	972	691	— 281
Poland	32.2 E.	Estimates 1930-31	33.4	28.1	17.2	10.9	—	28.1	252	273	+ 21
Portugal	6.2 E.	Estimates 1930-31	20.1	5.9	—	—	—	5.9	108	42	— 66
Roumania	18.0 C.	Estimates 1930	37.0	31.2	19.1	12.1	0.2	31.7	135 ¹	171 ¹	+ 36
Spain	23.6 E. ²	Estimates 1930 Cl. Accts.	102.7	—	—	—	—	—	472	444	— 28
United Kingdom of Great Britain and N. Ireland.	46.0 E.	1930-31 Cl. Accts.	1,771.7	176.5	140.5	36.0	—	176.5	4,661	2,778	— 1,883
Yugoslavia	13.9 E.	1930-31 Estimates	18.0	—	—	—	—	12.3	122	119	— 3
Australia	6.5 E.	1930-31 Cl. Accts.	287.1	—	—	—	—	—	435 ³	528 ³	+ 93
Canada	10.3 E.	1930-31 Cl. Accts.	201.8	25.0	21.2	3.8	—	25.0	1,008	886	— 122
United States of America	123.6 E.	1930-31 Cl. Accts.	1,050.9	—	—	—	—	—	3,120	3,782	+ 662

¹ Roumania. — Trade includes bullion.

² Spain. — Population includes that of Canary Islands.

³ Australia. — General trade. Includes bullion and specie.

Table VI.

**SUMMARY OF THE PRINCIPAL MEASURES ADOPTED SINCE SEPTEMBER 1st, 1931,
WHICH AFFECT INTERNATIONAL TRADE AND THE BALANCES OF PAYMENTS.**

(Compiled from information available to the Economic Section of the
League of Nations at the middle of July 1932.)

	September 1931	October 1931	November 1931
1. Abandonment of Gold Standard or Prohibition of Gold Exports	Bolivia United Kingdom Colombia Denmark Egypt India Irish Free State Norway Portugal Sweden	Canada Finland	
2. Control of Foreign Exchanges	Denmark Greece Hungary Persia	Argentine Austria Brazil Bulgaria Czechoslovakia Estonia Finland Latvia Turkey Yugoslavia	Bulgaria Czechoslovakia Estonia South Africa
3. Export bounties		South Africa	
Import Duties, Taxes imposed, Consular fees, etc.	4. General increase (all items)	India South Africa	Netherlands
	5. Increases on individual items	Argentine Colombia Egypt Italy Latvia Poland	Belgium United Kingdom Bulgaria France Persia
6. Import quotas or licensing systems		Brazil Latvia	Denmark Turkey
7. Milling regulations	Finland		
8. Import monopolies	Persia	Uruguay	Estonia
9. Import prohibitions	Colombia France	Latvia	
10. Moratoria on External Public Debt Service	Brazil	Bolivia	
11. Moratoria on External Commercial Debt Service	Uruguay		

Table VI (continued).

	December 1931	January 1932	February 1932
1. Abandonment of Gold Standard or Prohibition of Gold Exports	Japan	New Zealand (Gold coin not to be exported)	Costa Rica Ecuador
2. Control of Foreign Exchanges	Brazil Bulgaria Chile Italy Norway Venezuela	Czechoslovakia Nicaragua South Africa Turkey Yugoslavia	Denmark Nicaragua Roumania Spain Uruguay
3. Export bounties		South Africa	
Import Duties, Taxes imposed, Consular fees, etc.	4. General increase (all items)	Brazil	Norway
	5. Increases on individual items	United Kingdom Colombia Czechoslovakia Estonia France Lithuania Switzerland	Austria Colombia Germany Hungary Irish Free State Italy Poland Salvador Switzerland
			Australia ¹ Finland Persia Portugal Siam
			Belgium Estonia Germany Italy Lithuania Mexico South Africa Sweden Switzerland Venezuela
6. Import quotas or licensing systems	Estonia France Japan Latvia Netherlands Spain	Czechoslovakia Estonia France Hungary Netherlands	Denmark France Italy Latvia Persia Poland Portugal Switzerland
7. Milling regulations		Italy	
8. Import monopolies	Estonia		Sweden
9. Import prohibitions	Colombia Latvia	Poland	Latvia
10. Moratoria on External Public Debt Service	Hungary Uruguay		
11. Moratoria on External Commercial Debt Service			Germany

¹ Includes some reductions.

Table VI (continued).

	March 1932	April 1932	May 1932
1. Abandonment of Gold Standard or Prohibition of Gold Exports		Greece	Bolivia Greece Japan Peru Siam
2. Control of Foreign Exchanges	Austria Bulgaria Yugoslavia	Argentine Bulgaria Chile Czechoslovakia Ecuador Latvia	Roumania
3. Export bounties	Colombia South Africa	South Africa	
Import Duties, Taxes imposed, Consular, fees, etc.	4. General increase (all items)	Belgium United Kingdom Poland South Africa Venezuela	France U.S.A.
	5. Increases on individual items	Bolivia Brazil Egypt Estonia France Guatemala India Irish Free State Mexico Netherlands Roumania Salvador Spain	Belgium United Kingdom Canada China Egypt Irish Free State Italy ¹ Mexico Netherlands Spain Sweden Uruguay
6. Import quotas or licensing systems	Belgium Czechoslovakia France Hungary Netherlands Norway Roumania Switzerland	Austria Belgium Czechoslovakia Hungary Netherlands	Australia Austria Belgium ² Czechoslovakia Greece Hungary
7. Milling regulations	Czechoslovakia France ¹ Portugal	Italy ¹	
8. Import monopolies	Estonia	Estonia Latvia Switzerland	Estonia
9. Import prohibitions		Greece	
10. Moratoria on External Public Debt Service	Chile Salvador	Greece Latvia Yugoslavia	
11. Moratoria on External Commercial Debt Service	Chile Salvador Yugoslavia		

¹ Includes some reductions.

² For further details, see documents E.757 and supplements and E.780.

Table VI (concluded).

	June 1932	July 1932
1. Abandonment of Gold Standard or Prohibition of Gold Exports		
2. Control of Foreign Exchanges	Brazil Chile	Lithuania Poland
3. Export bounties'		
Import Duties, Taxes imposed, Consular fees, etc.	4. General increase (all items)	Japan Estonia Lithuania
	5. Increases on individual items	United Kingdom Denmark Egypt Germany Italy Norway Roumania
		United Kingdom Irish Free State U.S.A.
6. Import quotas or licensing systems	Belgium Hungary Switzerland	Austria France Hungary Latvia Switzerland
7. Milling regulations	France	
8. Import monopolies	Uruguay	
9. Import prohibitions	Greece South Africa	Turkey
10. Moratoria on External Public Debt Service		
11. Moratoria on External Commercial Debt Service		

The list above does not claim to give a complete picture of the measures taken to control international trade. It is compiled from information available at Geneva in the middle of July and may not include measures taken in distant countries in recent months. It does not include :

(a) The measures taken by nearly all countries with a view to exercising supervision over the trade in arms and war material, narcotics and certain products considered injurious to health, immoral literature, etc., or measures of protection against human or animal epidemics, diseases of plants, etc. ;

(b) The special measures regulating certain forms of trade between neighbouring countries (frontier quotas, etc.) ;

(c) The supervision of the export trade in certain goods to countries which have the system of " importation bonds " (Einfuhrscheine) or " exportation bonds " (Ausfuhrscheine).

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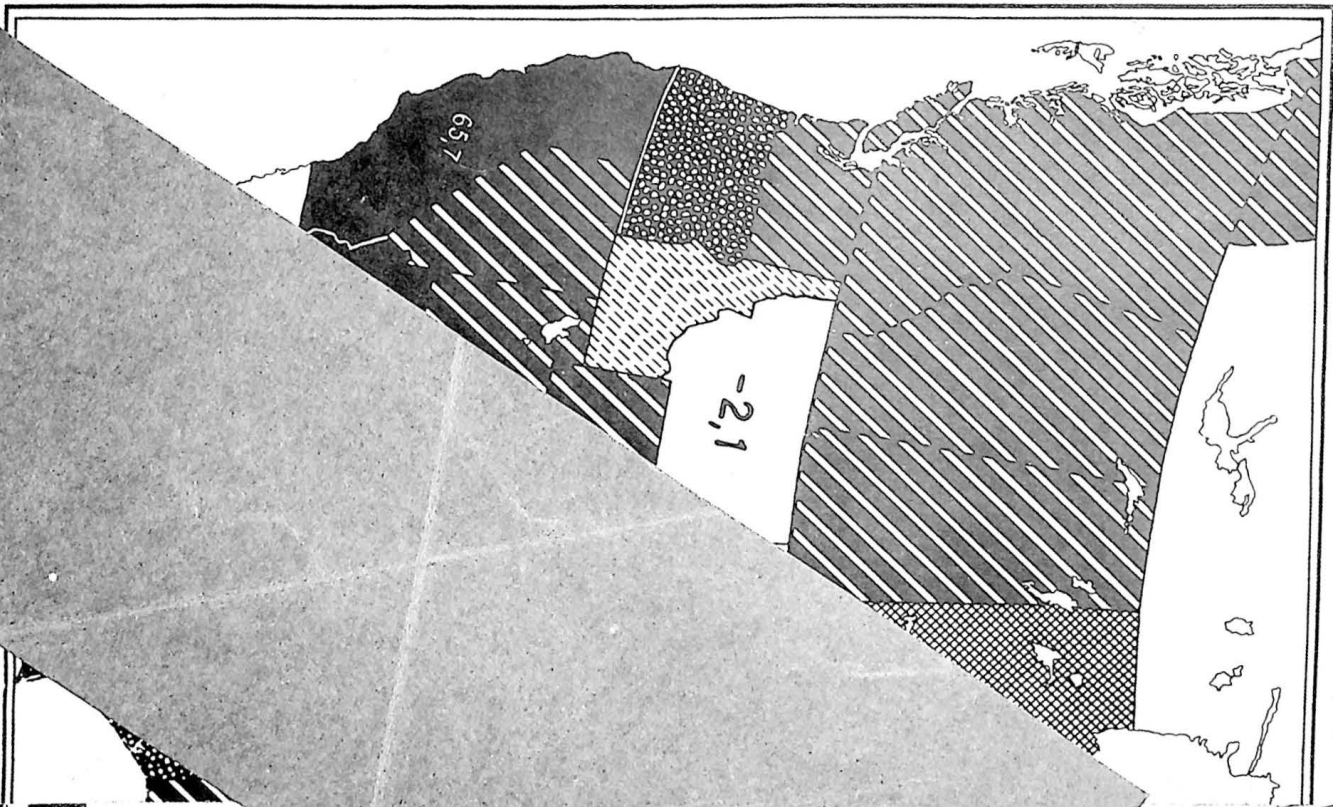
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The Increase of Population in Europe since 1920.

(The map below shows, for each administrative district, the decennial rate of increase between 1920 and 1930. The rate of increase has been estimated on the basis of the increase over a shorter period — for example, in Austria [1924-1929] and Greece [1921-1928].)

Augmentation de la population en Europe depuis 1920.

Taux décennal d'augmentation de la population entre 1920 et 1930.



Decennial Rate of Increase of the Population
Taux décennal d'augmentation de la population

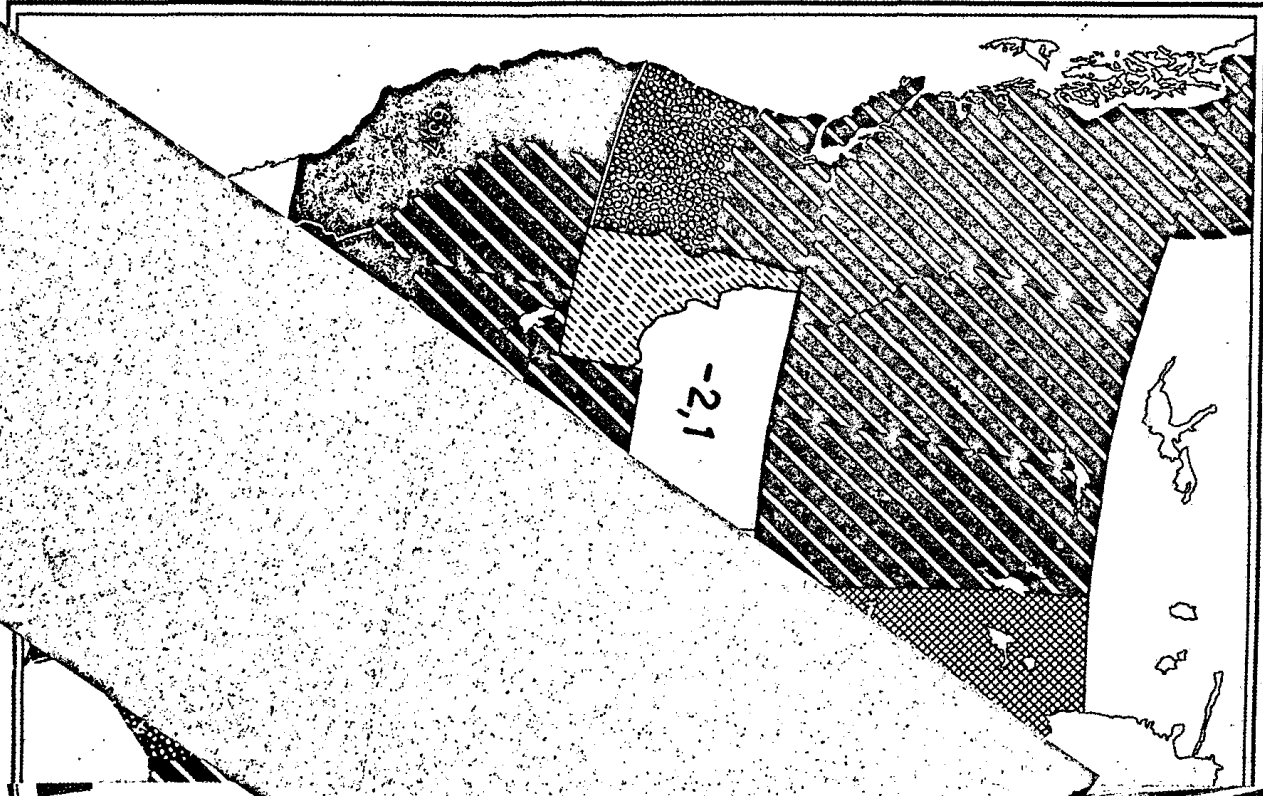


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ECONOMIC INTELLIGENCE SERVICE

**WORLD
ECONOMIC SURVEY**

1932-33

LEAGUE OF NATIONS

GENEVA

1933

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**Publications of the Economic Intelligence Service
of the League of Nations.**

MONTHLY BULLETIN OF STATISTICS.

STATISTICAL YEAR-BOOK OF THE LEAGUE OF NATIONS.

WORLD PRODUCTION AND PRICES.

REVIEW OF WORLD TRADE.

BALANCES OF PAYMENTS.

INTERNATIONAL TRADE STATISTICS.

COMMERCIAL BANKS.

WORLD ECONOMIC SURVEY

1932-33

PREFACE

The present *Survey* has been prepared by Mr. J. B. Condliffe, of the Economic Intelligence Service of the League of Nations. It is the second of an annual series undertaken in consequence of resolutions passed by the Assembly of the League in 1930 and 1931.

While this present work by Mr. Condliffe is based mainly on data collected by the Economic Intelligence Service of the League of Nations, valuable assistance has been obtained from other sources and particularly from the International Labour Office.

The book is intended to afford an account of recent developments intelligible to the lay reader. For more detailed and technical information, the reader should refer to the publications of the Economic Intelligence Service, a list of which is given on page 6.

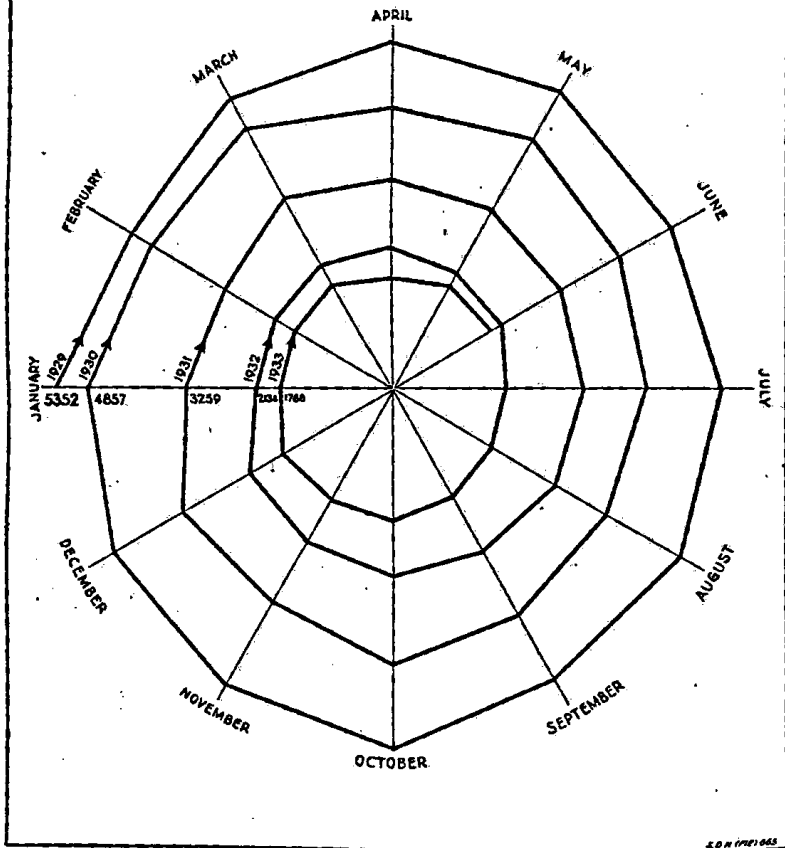
A. LOVEDAY,
*Director of the Financial Section
and Economic Intelligence Service.*

Geneva, August 20th, 1933.

THE CONTRACTING SPIRAL OF WORLD TRADE

Month by month January 1929-June 1933

(In millions of U.S. (gold) \$)



Note. — Cf. Monatsberichte des Österreichischen Institutes für Konjunkturforschung. Nr. 4, 1933, p. 63.

Chapter I.

A TROUBLED YEAR.

THE SCOPE OF THE SURVEY.

Any attempt to write a summary narrative of economic developments in a period when events moved as rapidly as in the year 1932 and the first months of 1933 must be to some extent unsatisfactory. The final chapter of the preceding *Survey* for 1931-32 was written in July 1932, at a time when there seemed some prospect of economic improvement. Subsequent months did not bear out the promise of revival. Prices declined again, international trade, and economic activity generally, became more restricted and the financial organisation of the world sustained a fresh series of blows in the early months of 1933. The chapters which follow have been written between the months of February and July 1933. During those months, events have moved rapidly. The American banking difficulties, and the departure of the United States from the gold standard, discussions concerning the future of war debt payments, and the opening of the Monetary and Economic Conference on June 12th, to say nothing of important developments in the political sphere, have created a situation which renders the task of the contemporary economic historian more than usually difficult.

The aim of the present *Survey*, however, like that of its predecessor, is to record events rather than attempt a final or even an interim judgment upon them. It is inevitable that some elements of judgment must enter into the selection, arrangement and analysis of the events recorded. It is impossible to record more than a fraction of the happenings of such a troubled period, and selection and arrangement are, of course, necessary; but, in selecting and arranging the material to be used, a few simple principles have been followed. Attention has been concentrated upon facts rather than opinions, upon decisions rather than plans, and upon the statistical evidence of economic activity rather

than upon legislation. Undue preoccupation with the dramatic financial developments in the great industrial countries has been avoided as far as possible and an effort has been made to view the whole world, rather than special areas, as the theatre of the developments to be described. No attempt has been made to present anything like a complete picture of national economic developments. Emphasis is laid rather upon the international aspects of these developments and illustrations are drawn from one country or another merely as they have proved accessible or convenient. There is, it is hoped, no national bias or prejudice either in the choice or in the presentation of such illustrative examples.

In such a troubled period, political forces exercise an influence upon economic development which no realistic survey of events can ignore. If these political forces are treated in the present volume only in so far as they throw light on economic problems, it is because there are many other sources in which a more adequate treatment may be found. The aim of this *Survey* is not primarily to diagnose causes or to weigh political and economic influences, but to record and interpret economic developments. The basic material for this purpose consists, not of parliamentary discussions, but rather of the statistics which reflect the economic activities of the business world. In the same way, no attempt is made to deduce conclusions or to suggest policies, though, at various points, certain problems emerge from the facts recorded.

In the main, the *Survey* deals with the year 1932 and the first half of 1933. The previous volume included some historical and analytical material which it is unnecessary to repeat ; but, where new topics have been dealt with, sufficient historical material is included to give an adequate background for the consideration of recent events. The present chapter is devoted to a rapid summary of the outstanding events from the summer of 1932 to the end of March 1933. The culmination of the American banking crisis at that time marks a significant division which it is convenient to observe. The chapters which follow analyse in more detail the developments of this period ending in March 1933. They are arranged by economic subjects rather than chronologically, but, as the frequent cross-references indicate, economic problems cannot be treated independently of one another. The arrangement of the chapters, beginning with Prices and continuing with Production, Wages, Profits, Public Finance, International Trade, Banking, Debts and Balances of Payments, follows an order which is logical, but is only one of many such arrangements that might have been chosen. The economic organisation of the world presents one great problem with many aspects, almost any one of which might reasonably be chosen as the point from which

to begin an analysis of the problem as a whole. There is, perhaps, a distinction, of degree rather than of kind, to be drawn between the first five and the last four subjects mentioned. The former are less, and the latter more, international, both in their material and in their implications. Indeed, the contrast between the persistency with which national organisation of the primary economic processes is maintained and the flexible adjustments of international equilibrium rendered increasingly necessary by the beginnings of an international financial system lies behind much of the present disturbance of the economic order. While any adequate consideration of this large problem lies outside the scope of the *Survey*, its manifestations are implicit in the facts recorded.

The final chapter is a sequel to the first, giving in rapid summary an outline of the principal events in the second quarter of 1933, and estimating the economic situation in July on the basis of such statistical and other evidence as was available at that time.

THE DEPTHS OF DEPRESSION.

In the early summer of 1932, economic activity in the world as a whole had touched depths unprecedented during the present depression, and international economic organisation was in a state of extreme confusion. It is still too soon, early in 1933, to be sure that the depths reached in the middle of 1932 were the lowest point. An improvement in the autumn was followed, particularly in the United States, by a further setback in the closing months of the year. Even during the brief period of improvement, there were persistent dragging factors of deterioration, especially the worsening of public finance, the burden of excessive debt, currency instability and a continued narrowing of international markets. In the last two months of 1932, these factors of deterioration appeared more clearly. But not all of the autumn improvement was lost when prices began to fall again and production lagged in the early winter. It is obvious that, in the second half of 1932 and the beginning of 1933, there were forces making for economic stabilisation, if not recovery; but they were held in check by obstacles which had piled up, or had not been cleared away, in the course of three years of depression. An examination of the economic situation in the middle of 1932 is therefore a necessary preliminary to any understanding of subsequent developments.

The facts of economic depression at that time were given in some detail in the *Survey* for 1931-32. Falling prices, declining production, vanishing world trade, accumulating debt, increasing unemployment had presented an almost unvarying and

melancholy progression for the better part of three years. There had been few and brief occasions when some slackening in the rate of decline had appeared to hold promise of stabilisation or return to more satisfactory conditions. Slight signs of improvement in the spring of 1930 and again in the early spring of 1931 had been overwhelmed by apparently irresistible economic pressure, and in May 1931 a financial panic began which was to shake even the most strongly organised countries and drive a great number off the international gold standard. As this panic swept from country to country, hurried measures of national economic defence were taken which inevitably resulted in further damage to the already weakened international economic connections. By the middle of 1932, the panic period appeared to be over; but an exhausted world was left to contemplate the ruin that had followed in the wake of the storm.

Two aspects of the damage caused by the financial panic need to be clearly distinguished. In the first place, economic activity, already at a low ebb after years of depression, was reduced to levels which could hardly have been deemed possible in the years before 1929. It would serve no useful purpose to reproduce again in great detail the statistical evidence of suspended economic animation in the summer of 1932. Production in most industrial countries appeared to reach its lowest point in the months of July and August, at levels ranging from about 25 per cent below peak production in the case of the United Kingdom to about 55 per cent below the peak in the case of the United States of America. The agricultural countries, particularly those in the southern hemisphere, did not suffer from decreased production in the same way, but, on the other hand, were hit very hard by the heavy fall in raw-material prices. Estimates of the reduction in national incomes caused by the combination of these factors are difficult to obtain; but in many countries the fall in the national income by the middle of 1932 seemed to be in the neighbourhood of 40 to 50 per cent.¹ Such an order of magnitude obviously indicates extremely difficult problems of income distribution and public finance.

Unemployment in the spring of 1932 was conservatively estimated by the Director of the International Labour Office as directly involving at least twenty-five millions of workers. International trade in the first half of 1932 had fallen to less than 40 per cent of its value in the first half of 1929.² World stocks of raw materials had continued to pile up until they were in the aggregate approximately double what they had been in

¹ Cf. estimates given in Chapter IV.

² Cf. Chapter VII.

1925.¹ Unemployed workers and factories were matched by unemployed capital. The Bank for International Settlements estimated the short-term credit which had accumulated in the money markets of the world at 50 milliards of Swiss francs. Further statistical estimates might be quoted ; but there is little need to emphasise the low ebb which economic activity had reached in the middle of 1932.

What was even more serious than the damping down of economic activity in almost every direction was the disorganisation and partial destruction of the delicate machinery of international economic and financial co-operation. There were a great many indications of national economic and financial disorder ; but, serious as these were, they were probably less dangerous for the future than the disruption of international economic equilibria. It was the decline of international trade to a mere fraction of its former value, the stoppage of the circulation of capital, and exchange instability, all of which were part cause and part effect of the disorder into which the balances of international payments had fallen, which offered the most difficult obstacles in the middle of 1932 to any lasting revival of economic activity.

It is not suggested that these aspects of breakdown should be regarded as the ultimate causes of the depression. They were rather symptoms, the causes of which are to be sought in earlier and more fundamental phenomena. At the stage which the depression had reached in mid-1932, however, exchange instability, restricted trade, disorganised capital markets and the general disturbance of equilibrium between national price systems threatened to become in their turn a cause of further depression.

All of these aspects of breakdown, it should be emphasised, were practically worldwide. When the United Kingdom abandoned the gold standard in September 1931, every creditor or debtor in any country who held British or foreign contracts in terms of sterling and all traders in the British market were immediately affected. Almost simultaneously, a great number of other countries left the gold standard and this circle widened constantly. Depreciation of the exchanges below the sterling level became a serious problem in countries as far apart and as different in economic structure as Greece, Chile, Japan, Australia and New Zealand. Later, in January 1933, New Zealand's action in lowering her exchange rate to Australia's level was followed within a few days by similar action in Denmark.

¹ Cf. Chapter III.

The other aspects of breakdown could be illustrated equally well by examples drawn from very different quarters of the globe. The number of countries cited below as imposing trade restrictions is fair evidence of the universality of this method of economic defence.

The stoppage of capital movements, the freezing of short-term indebtedness and difficulties in balancing international payments also were problems by no means confined to a few European countries. By the end of 1932, there were moratoria on the foreign service of the public debt in seventeen countries and moratoria on private debt service in seven others. Apart from the countries which had resorted to this extreme step, there were many others, particularly among the agricultural countries of the southern hemisphere, which found the fiscal burden of external debt payments, already a crushing proportion of their shrunken export values, increased very considerably by the depreciation of the external value of their currencies below that of the currencies in which their debts were held.

It is difficult to discuss the phenomena presented by this vicious circle, in which trade restrictions, declining trade, distorted balances of payments, frozen debts and exchange instability reacted unfavourably one upon the other, in any order which does not give a misleading impression of priority and causation. The historical events which led first to economic strain and then to financial panic were treated in the first two chapters of the *Survey* for 1931-32. Stress was there laid upon the intricate and complex action and reaction between the various phenomena that lay behind the breakdown. International trade was declining, international investment had virtually ceased and the balancing of international accounts was becoming increasingly difficult long before the financial panic swept so many currencies off the gold standard. The breakdown of the international monetary standard was an effect rather than a cause of these difficulties.

It is arguable indeed that the widespread abandonment of the international gold standard relieved the situation, at least temporarily, by reducing the burden of external indebtedness of many countries in so far as their debt was held in terms of the currencies that were depreciated. Those whose domestic currencies for various reasons went on to depreciate below the level of the currencies in which their debts were due, on the other hand, found their external burden increased. Whether the economic situation in the middle of 1932 would have been better or worse if the gold standard had not been abandoned so widely is an academic question to which no answer need be attempted here. But it is at least clear that the sequence of

events summarised below cannot be ascribed solely to the abandonment of the gold standard. It is probable that trade would have continued to decline during 1932, prices to fall and investment to remain paralysed, if it had proved possible to retain the gold standard. These things were happening before the breakdown of that standard and were indeed among the causes of its breaking down.

At the same time, it is equally clear that the addition of widespread exchange instability to the ills from which the world was suffering greatly complicated the situation. Currency devaluation or depreciation by a single country to a fixed point followed by stabilisation and the achievement of new international equilibria is a different proposition from the inauguration of a period of unstable exchanges during which it is impossible to do international business on any rational basis because the relative scales of value are constantly changing. The most destructive development during 1932 was exchange instability. The capacity of one country to sell in another's market, or its potentialities as a market for the other's exports, to say nothing of the valuation of its international debts or credits, was likely to be changed quickly and radically by fluctuations in the rates at which the different currencies could be exchanged.

Fluctuating exchange rates aggravated by speculation and non-economic capital movements, the possibility of international competition in cutting export costs by allowing currencies to depreciate, hurriedly improvised but drastic measures of trade restriction thrown up partly as a defence against such competition, renewed deflationary pressure and banking crises and rigid exchange controls to protect the weaker currencies against this fresh derangement of international economic equilibria had created a thoroughly unstable situation by the middle of 1932. The uncertainties of such a situation were not only a serious obstacle to economic recovery, but presented a constant threat of further deterioration. More than half the countries of the world had formally abandoned the gold standard and most of the others maintained it, or its semblance, only by rigid exchange controls. Only a handful of countries were able to retain a free gold standard. The countries off gold, while their domestic situation had been temporarily relieved, were confronted by an accelerated fall of gold prices and a further drastic curtailment of trade. On the other hand, their efforts to hold the external values of their currencies stable were menaced by flights of capital which were apt to assume large proportions suddenly as the security of one financial centre or another appeared to be enhanced or jeopardised. The relief obtained from the abandonment of the gold standard by the countries off gold

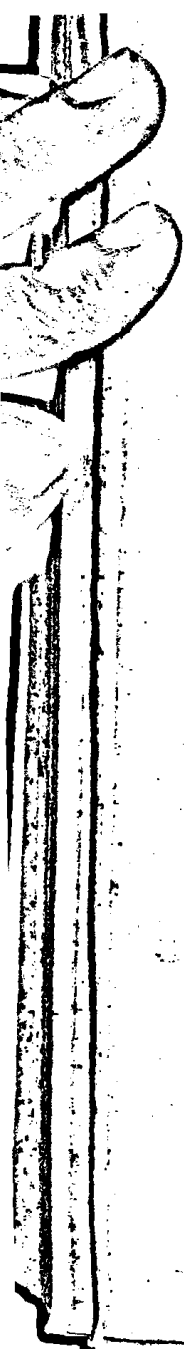
and by the world as a whole therefore proved disappointing. Prices did not rise and trade was drastically curtailed, while exchange instability and exchange controls imposed fresh obstacles to capital movements. The course of prices in both gold and paper standard countries is analysed in a later chapter. Here it is sufficient to state that, after an initial rise in paper prices as each country left the gold standard, these paper prices began to fall again in conformity with the downward drift of the gold price-levels.

Both the volume and the value of international trade, already seriously diminished before the financial panic, shrank still further. In the third quarter of 1932, the value of world trade was less than 35 per cent of what it had been in the corresponding quarter of 1929. The decline was not evenly distributed, since the prices of raw materials and agricultural products generally had fallen more than those of finished manufactures, so that the countries exporting mainly raw materials were specially hard hit. At the low point in the third quarter of 1932, the international trade of the European countries fell for the first time below 40 per cent of the 1929 level, while that of the rest of the world, including North America, fell below 30 per cent.

There were two elements in this decline, the fall in average prices which appears to have been about 50 per cent, and a reduction of about 25 per cent in the actual quantum of goods exchanged. The exchange of three-fourths of the former quantity of goods, at about half the prices ruling three years before, yielded a total value of world trade little more than a third of the 1929 monthly average.

Both of these elements were largely due to the progressive constriction of world markets by the imposition of emergency trade restrictions to meet the financial panic. The multiplicity and variety of these emergency restrictions after September 1931 is difficult to summarise in a few words, but a survey made at the end of 1932 yielded the following main conclusions. Thirty-five countries were off the gold standard¹ and twenty-seven, including nine that were nominally still on the gold standard, were officially exercising exchange control, while unofficial controls were employed in three other countries, and, in some which remained theoretically on the unrestricted gold standard, the control of commodity imports by prohibitions was virtually equivalent to an exchange control. In the sixteen months after

¹ League of Nations : *Monthly Bulletin of Statistics*. Cf. also *Index*, Vol. VIII, No. 85, January 1933, pages 6 to 13, and Samuel Montagu & Co.'s *Weekly Review*, January 5th, 1933. The exact number is difficult to determine, since the position of several countries, while legally unchanged, is in fact modified.



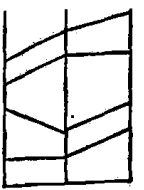
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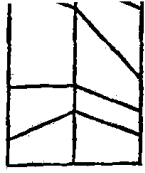
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Diminishing improvement

Upward turn



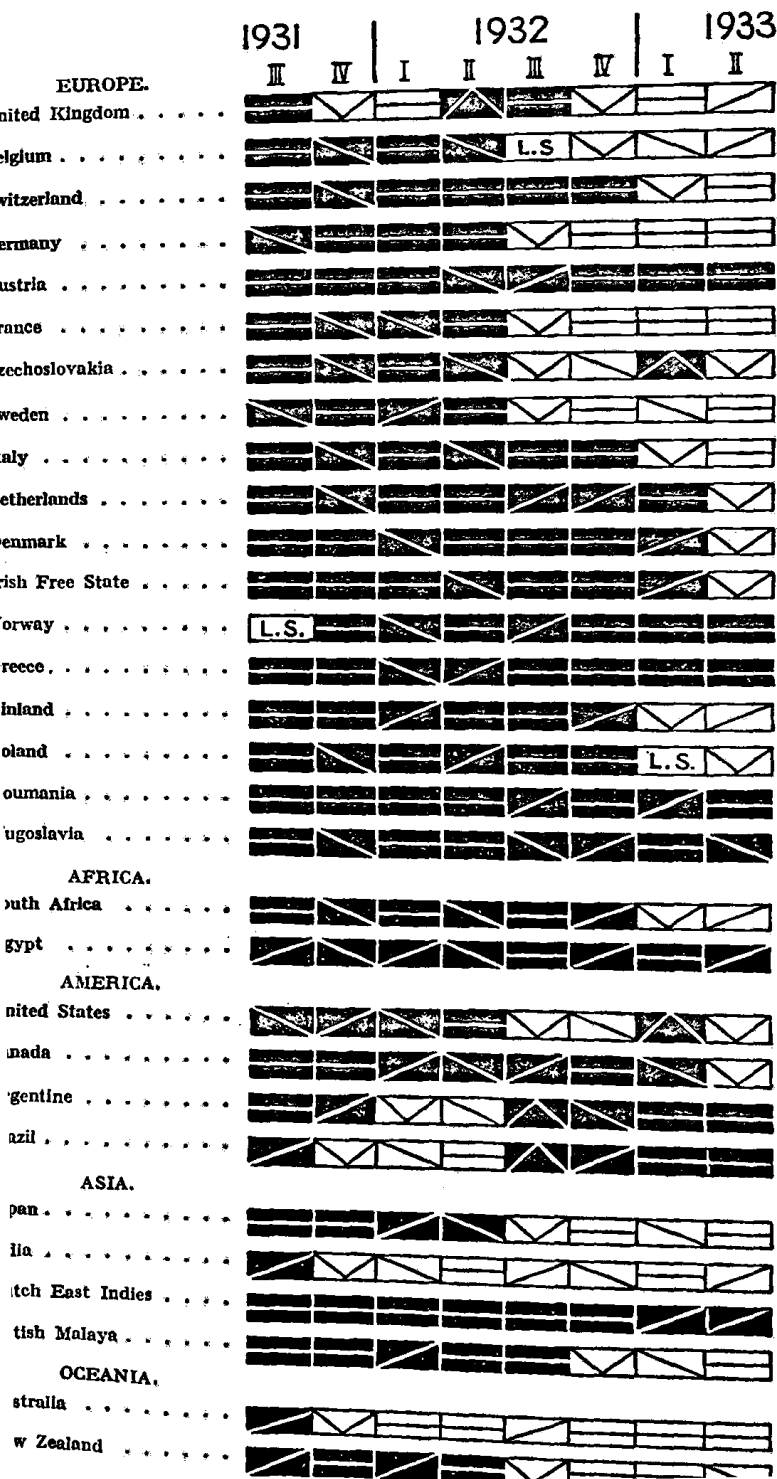
Preceding quarter Actual quarter

aggravation

Accelerating aggravation

Downward turn

Preceding quarter Actual quarter



September 1st, 1931, general tariff increases had been imposed in twenty-three countries, in three of them twice during the period — with only one case of a general tariff reduction. Customs duties had been increased on individual items or groups of commodities by fifty countries, in most cases by a succession of enactments which, in several countries, numbered over twenty tariff changes in the sixteen months. Import quotas, prohibitions, licensing systems and similar quantitative restrictions, with even more frequent changes in several important cases, had been imposed by thirty-two countries. Import monopolies, for the most part of grains, were in existence in twelve countries; milling or mixing regulations in sixteen others. Export premiums were being paid in nine, while export duties or prohibitions had been imposed in seventeen.

This bare list is utterly inadequate to portray the harassing complexity of the emergency restrictions that were superimposed upon an already fettered world trade after the period of exchange instability was inaugurated by the abandonment of the gold standard by the United Kingdom in September 1931. By the middle of 1932, it was obvious that the international trading mechanism was in real danger of being smashed as completely as the international monetary system had been.

The circulation of capital both on long and on short term had been impaired early in the depression; but, by the middle of 1932, the financial panic had brought about an almost complete paralysis of capital movements and had gone far to impair the service of existing debt in many countries. Over-indebtedness had induced an increasing number of countries to impose rigid exchange controls, in an effort to preserve currency stability. The steady diminution of international trade referred to above was largely responsible for this and for the "freezing" of short-term debts, since amounts of short-term indebtedness adequate to finance trade in its 1929 volume became redundant, but difficult to repatriate, when trade fell to 1932 levels.

In the middle of 1932, therefore, there was a widespread realisation of the serious extent to which the international economic and financial system had broken down. The fear was freely expressed that the breakdown might become irreparable. To the decline of activity and the confusion of relationships, there was added general pessimism and fear of a more complete collapse. Yet, within a few months, despite the persistence of economic conditions that were on the whole little better and in some respects even worse than in the summer, a feeling of confidence began to return and the number of experts willing to believe that the bottom of the depression had been touched steadily increased. The turning-point, psychologically, if not

economically, came in the late summer. During the autumn what was popularly known as a "boomlet" developed in the United States, and, though subsequent experience was chastening, the undercurrent of optimism, not wholly unwarranted by actual experience, persisted into 1933.

A LIMITED AUTUMN REVIVAL.

One of the characteristic features of such a troubled year as 1932 proved to be is the uncertainty of statistical measurements that could formerly be relied upon to indicate with fair precision at least the general trend of economic events. With the common measure of value abandoned over a great part of the trading world, and the normal mechanism for restoring equilibrium largely broken down, the interpretation of statistical guides and indices became much more speculative. Economic statistics are always relative; but, in 1932, widespread exchange instability made their interpretation still more difficult. Not only were there many elementary pitfalls such as quotations in the same unit of currency as before meaning very different things because that currency had depreciated, but the subtler effects of such depreciation were apt to escape notice in many different directions. For example, the price of representative international bonds which were formerly quoted in the main financial centres at prices which did not differ by more than the cost of transmitting gold, after the abandonment of the gold standard, differed, even between free exchange markets, by margins which, at the low prices current, represented up to 1 per cent difference in the yields of the bonds. Such wide differences were due almost wholly to the expectation of movements in the foreign exchanges changing the relation of the currencies in question. In the same way, the constriction of international trade, the paralysis of the international capital markets, the uneven fall in prices both as between different commodity markets and internationally, all made the interpretation of current statistics by pre-depression conceptions a hazardous procedure. There were particular difficulties in the case of index-numbers and the use of percentages generally. A rise in prices or an increase of production measured as a percentage of the extremely low levels reached in mid-1932 appeared to be a much more substantial measure of recovery than if the same small rise was measured as a percentage of the boom levels of 1929 or even the levels of mid-1931. There was more than merely statistical difficulty involved in this problem of measurement. If every part of the economic organisation had been adjusted to the levels of prices ruling at the low

point in mid-1932, a rise of say 10 per cent from that low point might have been regarded as very encouraging. But in so far as many parts had remained fixed somewhere between 1929 and 1932 levels, such a rise, which, on the 1929 basis, was only a fraction of 10 per cent, might well appear entirely inadequate to presage a general recovery.

In any attempt, therefore, to estimate the significance of the somewhat confused economic tendencies in the latter half of 1932 and the first months of 1933, there must inevitably be a considerable margin of uncertainty and many qualifications. A day-to-day interpretation of current events built up a general notion of revival in the autumn of 1932, followed by a substantial set-back in the closing months of the year. The results of the year 1932 as a whole were generally interpreted in the reviews of early 1933 as not unsatisfactory, in the sense that the lowest depths appeared to have been reached and the worst experiences survived. This rather more confident note was perhaps clearest in the countries which had abandoned the gold standard, and particularly in the United Kingdom which entered 1933 with a strong upward pressure on her currency. Even in the United States, which, of all the gold countries, was hardest hit at the turn of the year, there were not wanting expressions of confidence that, for some months, economic activity had been "bumping along on the bottom" of the depression. It is obvious, however, that such interpretations must necessarily reflect the prevailing business tone rather than exactly measurable facts. There seems little doubt that, for two or three months after July 1932, business confidence rose in almost every country; but that the events of succeeding months, from October onwards, had a sobering effect and that the revival of confidence was progressively checked thereafter. There was in the early months of 1933 little sign of over-optimism, but rather a mixed attitude of hope that the worst was past and of fear lest delayed recovery might open up still worse cracks in the economic system.

The substantiation or correction of this interpretation of current events by somewhat later analysis of the available statistical information is not altogether an easy task. As the following chapters bear ample witness, the course of production, prices, trade and other economic phenomena was extremely confusing in this period. In the pages which follow, however, an attempt is made to set out briefly the major qualifications which need to be made before accepting the current notion of autumn revival and later setback. The more detailed justification of these qualifications will be found in succeeding chapters.

The most substantial gains in the autumn of 1932 were registered in the security markets, which rose sharply, especially

in North America and the United Kingdom, during August and September. There were substantial advances recorded in the average levels of wholesale commodity prices in the same countries during these months. A definite increase in the value and volume of industrial production began in most countries about this time and the total value of world trade rose from July to October also. Unemployment is much affected by seasonal fluctuation, but the autumn decrease and summer increase, when corrected for seasonal variations, appeared in many countries to show improvement which was correlated with the upward tendency in production and with some indications that raw-material stocks were moving from producers to manufacturers. These were the principal signs of such economic improvement as took place in the autumn and early winter. Their significance and duration warrants closer statistical analysis in an effort to discover the main reasons for improvement, its limits, and the causes of the later setback.

The exact date of the turn differs from country to country, but the monetary and financial changes appear to have generally, though not invariably, preceded the improvements in production. The first recognisable sign of recovery, apart from the stabilisation of banking conditions referred to later, was a halt in the falling tendency of commodity prices. Many important commodities had touched their lowest points in the first half of 1932, and the prospect of commodity prices rising again may well have been an important element in the advance of the security markets. The average levels of wholesale prices, but not all prices, nor the average in all countries, began to rise about July ; but the rise was most marked in the United States and in some of the countries off gold. There were several important commercial countries, however — France, Germany, the Argentine, Dutch East Indies, Poland — where the decline in prices continued unchecked, and many others where the rise in July and August was very slight.

A fairly general revival in the prices of fixed interest-bearing securities was apparent in continental gold countries — Belgium, France, Switzerland — as early as June. There had, indeed, been a very substantial rise in French security prices in February, caused apparently by a flight of capital to France when the financial panic was at its worst in the United States. This movement, like the sustained rise of British securities at the end of the year, illustrates the difficulty of interpreting world events from the limited viewpoint of one market. In July, however, there was a widespread upward movement of fixed-interest security prices in many markets, notably in Germany, Canada, the United States and the United Kingdom.

The improved credit of the British Government enabled it to take advantage of the accumulation of credit and lower interest rates to carry through vast conversion operations. On June 30th, at which date the bank rate was lowered to 2 per cent, the first great operation was launched by which £2,087 million of 5 per cent War Loan was converted to a 3½ per cent basis. The operation closed at the end of September and was a great success, all but 8 per cent of the total loan being converted. The remainder was paid in cash without difficulty on December 1st. The British Government followed up this initial success with other smaller operations and, in October, the Australian Government, which had earlier converted its domestic debt and lowered interest rates, converted the first instalment (£12 million of New South Wales 5¾ per cent Stock) of its external debt to a basis of 4½ per cent. Commercial issues followed early in October and the reduction of long-term interest rates facilitated commercial conversions as well as new capital issues. Building societies and other financial institutions reduced their interest rates, and there was a general tendency to look for further reductions in long-term interest rates.

The movement thus initiated in London spread to other financial centres. In September, the French Government, despite a difficult budgetary situation, was able to convert all but 2½ per cent of 86 milliard francs of Rentes and Treasury bonds carrying interest at 5, 6 and 7 per cent, to a 4½ per cent basis. On October 1st, the rate of interest paid on deposits in all Italian credit institutions was reduced, and similar arrangements followed in Czechoslovakia and other countries. Germany had already reduced interest rates and New Zealand, early in 1933, successfully converted £115 million of domestic debt.

The general lowering of long-term interest rates, illustrated by these operations in widely separated countries, was one of the most important financial gains from the more confident atmosphere in the summer of 1932. Not only were budgetary burdens lessened, but the price of fixed-interest securities rose sharply and the rise spread also to high-grade commercial bonds.

After October, there was a considerable setback in the United States and Canada ; but in most European countries, and especially the United Kingdom and Germany, the upward movement continued into 1933. The rise in Germany was abruptly arrested in the middle of February, but the British market, strengthened by a renewed flight of capital from both France and the United States, continued firm.

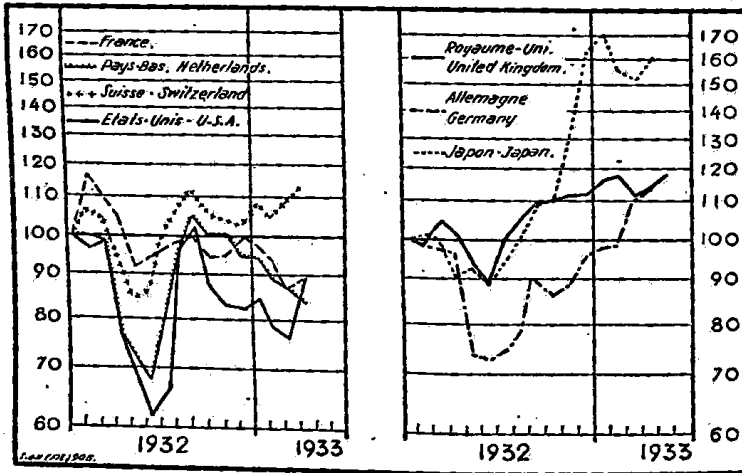
The index-numbers which measure economic, as distinct from financial, progress, particularly the statistics of industrial production, did not begin to rise till August. Their movement was the last in the sequence, but it continued in most countries into

November. Decline set in once more in the United States in November and, even allowing for seasonal fluctuation, most other countries showed declines in December. The increased production, which had been caused largely by progress in industries, such as the textile group, producing consumers' goods, did not long survive whatever stimulus had brought financial optimism in the autumn.

The accompanying diagrams bear witness, not only to the relatively slight degree of the autumn revival, but also to its uneven character in the different countries for which information is readily available. The successive peaks of security prices in different markets in recent months — London in December 1931, Paris in February, New York in October, Berlin and London in December 1932 and London in February 1933 — suggest very strongly that a large part of the fluctuation is due to capital movements. Only in the period July to October was there a general tendency to rising values in all the markets considered. The rise in commodity prices came a month earlier but was not so general. The improvement in production came a little later. It is evident that the factors which caused the revival found expression in June and July, and that their impetus varied greatly from country to country, but was largely spent by the end of the year.

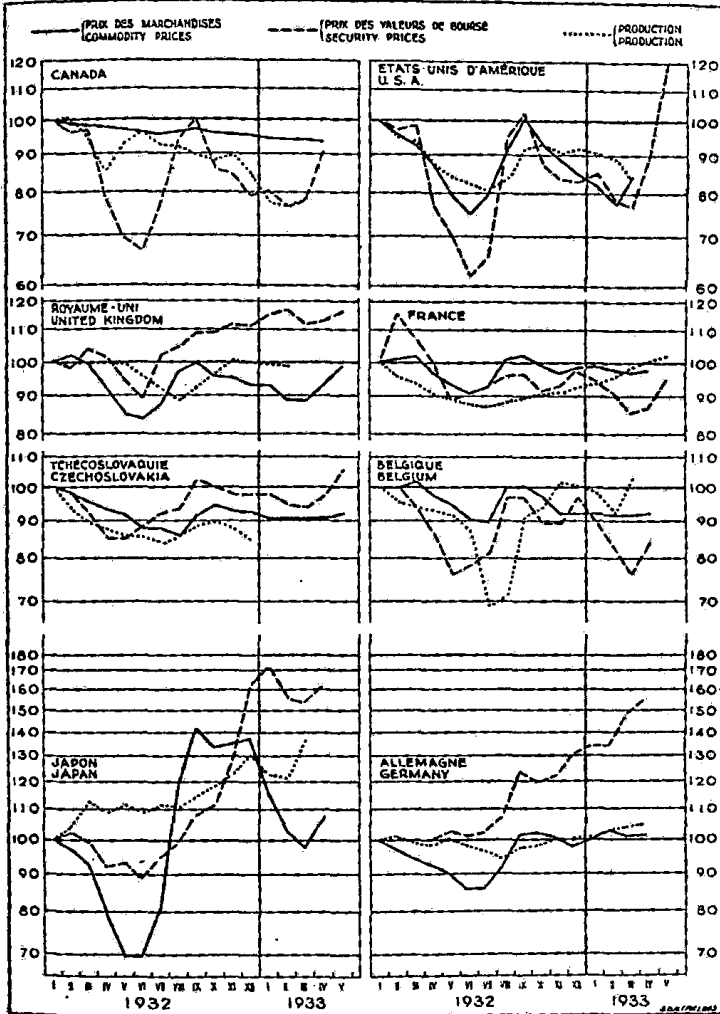
The extent of the revival from the low point in July to the high point in October may be roughly measured by the following diagrams :

Industrial Security Prices in Main Financial Centres.
(Base : January 1932=100.)



*Prices, Industrial Security Values and Production,
January 1932 to June 1933.*¹

(Base : January 1932=100.)



¹ The price indices are the national indices of sensitive prices except in the case of the United Kingdom, France and Canada, where the textile group of the general wholesale price indices has been given as being the most sensitive price group. In the case of Japan, the price curve represents the average of wholesale prices. The industrial security value and production indices are those national indices given in the League of Nations *Monthly Bulletin of Statistics*.

The stage had been set for the autumn revival by a combination of monetary and financial factors which may be broadly summed up as a return to more normal conditions after the financial panic which raged from May 1931 and was especially severe after the United Kingdom abandoned the gold standard in September of that year. The intense deflationary pressure which was caused by the panic was gradually eased in the case of the countries abandoning gold by the stability of their internal price-levels, achieved partly by using the exchange rate as a buffer against falling prices, and in the case of the gold-standard countries by a gradual return of confidence following the successful resistance of most financial institutions to the strain of the liquidity crisis.

In the early summer of 1932, some progress had been made in many countries towards establishing a new equilibrium between costs of production and prices. In nearly all the countries which remained on the gold standard, there had been strong deflationary pressure expressed by economies in government expenditure, reductions of wages, and, in some cases, of interest, rents and fixed charges, and by forced capital reconstruction through bankruptcies. Such measures were undertaken also in many of the countries that had abandoned gold, notably in Australia. The very fact of depreciating the paper currencies, thus making possible some initial rise of wholesale prices without a corresponding increase in costs of production, was an important method of readjustment. When the worst of the financial panic was over and the relief gained from such readjustments became noticeable, there was a breathing space of a few months before the secondary results of the monetary breakdown became apparent. During those months, the financial and banking situation improved sufficiently to encourage the expectation of renewed economic activity and rising prices. In most of the important commercial countries, commercial bank deposits reached their lowest point and began to expand again between February and July 1932. It is true that this expansion does not tell the whole story, since the rate of turnover or, to use the technical expression, the velocity of circulation, continued to decrease. In itself, however, it was a favourable development and one which encouraged the hope of an improvement in confidence leading once again to a more rapid turnover.

This temporary strengthening of the banking situation was mainly due to the inherent powers of resistance shown by the commercial banks in the panic; but, in the United States, it was assisted by the activities of the Finance Reconstruction Corporation in making short-term advances to banks and other commercial institutions which, though reputed solvent, were

exposed to sudden runs. The combined efforts of the Reconstruction Finance Corporation and the Federal Reserve Banks had by mid-1932 temporarily stayed the worst of the financial panic. The bulk of the assistance given to the commercial banks was used to repay their indebtedness and so to strengthen their liquid resources rather than to extend their operations; but, as their position improved, the pressure on the security markets caused by forced sales tended to diminish. Assistance given to railways and similar enterprises had much the same effect.

At the same time, there had everywhere been continuous and effective re-organisations and adjustments of private business. The manifold forms taken by such re-organisation cannot be summarised briefly, but it is obvious that business men, individually and collectively, had not been idle in face of the depression. Economies great and small, the introduction of improved methods of production, reductions and re-arrangements of staff were extended and were paralleled by collective action to reduce costs.

Continuous efforts were made also to organise restrictions and control of production — *e.g.*, in the petrol industry in the United States, where the price of gasoline was stabilised early in 1931. Such developments, either by formal arrangement or by a natural shrinkage of production in the face of adverse prices, extended during 1932. A tabulation of the minimum points reached by the prices of important commodities shows that, in a number of commodities, the upward turn took place about the middle of 1932.

For a short time, it appeared as if the intervention of the Federal Reserve Banks and the Reconstruction Finance Corporation had arrested the spiral of deflation in the United States and might go on to stimulate an upward movement of prices and production; but the open-market operations which had made this policy possible were stopped in August. The new economic policy launched by the German Government at the end of August combined remission of taxes with reductions in wages, but was put into operation cautiously. The British and French conversion operations were successful in achieving a reduction in governmental expenditure and also in making the first breach in the high rates of long-term interest, which were a burden both to national budgets and to industry.

All of these steps, however, important as they were, fell far short of the widely advocated policy of "controlled reflation", and were indeed conducted simultaneously with deflationary policies in other directions. The exact extent to which they were responsible for the autumn revival must be a matter of

conjecture. There were other factors at work at the time, notably a speculative anticipation of economic recovery largely based upon the hopes of improved international co-operation as a result of the Lausanne Conference.

THE DOWNWARD DRIFT.

The statistics of recovery examined in the preceding section are necessarily measures of national progress in the principal countries for which statistics are readily available. Inevitably these are the industrial countries of Western Europe and North America. The agricultural countries of the world, particularly those more remote from Europe, though equally bound up in the world economy, do not always share the economic changes that are apparent in the industrial countries. At best there is a long time-lag before such changes are fully registered.

The autumn revival in Europe and North America, it has been shown, was of a limited character, both in range and in time. It did not extend equally to all countries or to all industries and, by the end of the year, its impetus had been spent. The measure of economic readjustment that had been reached in the course of the depression had opened up the possibility of some recovery both in prices and production, the measures taken to arrest the liquidity crisis in the United States had eased the deflationary pressure in that important country and the improved prospects of international action that seemed apparent after Lausanne had contributed to a more confident tone in the speculative markets.

The agricultural countries appear to have anticipated the industrial countries in adjusting their domestic economic difficulties after the financial crisis. Almost all of them had abandoned the gold standard, thereby gaining relief in their domestic obligations while, at the same time, finding their external obligations lessened except when their domestic currencies fell below the level of sterling or other currencies in which their debts were due. Many of the agricultural countries also had supplemented these substantial reliefs by vigorous measures of domestic deflation. They were aided by the first rise in sterling prices after the abandonment of the gold standard, a rise which was substantial and lasted into the first quarter of 1932, long enough to cover most of the export season in the southern summer. It is not surprising, therefore, to discover widespread evidence of improved economic conditions in many raw-material-producing countries, particularly in those of the so-called "sterling group" in the first half of 1932. There is good reason to believe that

this improvement, in turn, was a substantial factor in the revival of the industrial countries later in the year. Increased purchasing power in the agricultural countries, particularly those which have not imposed extraordinary restrictions upon imports, is obviously favourable to an expansion of exports and therefore of production from the industrial countries.

At this point, however, in the middle of 1932, despite the more hopeful outlook in Europe and the United States, the secondary effects of the breakdown of international economic co-operation began to undermine the hopes of recovery.

Before the full effect of the autumn recovery could penetrate to the raw-material-producing countries, the first stimulating but evanescent consequences of currency depreciation had been succeeded by the depressing renewal of the decline in prices, which was aggravated by the uncertainties and restrictions of a broken international system. The autumn revival came too late and was too limited to prevent the renewed pressure on the weaker countries from once again breaking through the partial stabilisation that had almost been attained. Moreover, it was based, not on a genuine removal of the outstanding obstacles to recovery and a reconstruction of the broken international mechanism, but merely upon spurts of revival in isolated areas based in part upon dubious stimuli and upon the hope rather than the fact of reconstruction.

Exchange instability, trade restrictions, and the absence of capital imports, together with the recurrence of a falling price tendency in the second quarter of the year, limited the expansion of purchasing power that had been in progress in the agricultural countries. Many of the exchanges that had hitherto been stable or showed encouraging signs of regaining a measure of stability after the abandonment of gold parities began to drift downward again. There were signs of weakness in several South and Central American currencies early in the year. The Bolivian and Mexican exchanges fell in the early part of the year and were followed later by the Venezuelan, Peruvian and Chilean. On the other hand, the exchanges of Uruguay, Brazil — and, later, of Mexico and Venezuela — rose somewhat. Sterling and all currencies associated with it weakened steadily from April till December. The Greek drachma fell precipitately in April also and in June Ecuador was a new addition to the list of the countries with depreciated exchanges. In December, South Africa, after a long struggle, abandoned the gold standard and the next month the New Zealand pound dropped from 10 per cent below sterling to parity with the Australian currency at 20 per cent below. The Danish krone fell almost immediately to the same level and there was strong pressure on the Canadian dollar also.

Throughout 1932, the Japanese yen had been falling and in February 1933 it displayed renewed weakness.

Such widespread currency instability was paralleled by a stiffening of exchange controls in those countries which still maintained a nominal gold parity. Both phenomena provided evidence of severe strain upon the balances of international payments. Currency instability in turn aggravated the severity with which restrictions were imposed upon international trade and made impossible any hope of restoring the circulation of capital. The maintenance, except for a short time in the autumn, of huge stocks of primary commodities as international trade shrank, and the growing tendency towards the isolation of domestic markets, imposed renewed pressure upon the general level of prices, which began once again to decline steadily. Gold prices which had been rising from the middle of June began to fall again in the middle of September, lost all the autumn gains by early December and went on falling steadily in the early months of 1933. Sterling prices also fell from September onward, but not so sharply, part of the pressure being taken by a substantial fall in the exchange rate, which, however, throughout the whole period after the breakdown of the gold standard, had been the forerunner of further declines in the gold price-level.

Thus the economic situation was threatening in the early months of 1933 to develop into a still more serious phase of the financial depression. Despite the great and not wholly unsuccessful efforts made by a multitude of individuals and many Governments to bring order into the national economic situations, the breakdown of international commerce, finance, and currency was dragging all the nations down and imposing a strain on the weaker countries that threatened to become intolerable. At the turn of the year, production and prices were declining again almost everywhere. Unemployment showed little sign of decreasing. International trade had resumed its downward drift and fell more steeply still in January. Stocks of staple commodities remained very large. National incomes fell to even lower levels and the difficulties of public finance inevitably increased. Most ominous of all, there appeared in more than one country the weakening of exchanges and rising tendency of domestic prices premonitory of currency inflation. The detailed measurement of these various symptoms of deterioration will be set out in later chapters.

In the early months of 1933, therefore, the vicious circle was complete again. Competitive deterioration of the economic situation was well under way, as every country sought to protect itself at the expense of its neighbours. The tragedy of the

depression, repeated again in the autumn of 1932, has been that accommodation to international necessities has been too grudging and has come too late to avert further deterioration in the weaker countries, thus entailing a new and more difficult effort at restoring equilibrium at still lower levels.

THE BEGINNINGS OF INTERNATIONAL ACTION.

It is not without significance that the psychological, and possibly the economic, beginnings of improvement coincided with the first constructive efforts at international action to remedy the depression and that the economic situation grew worse again as the hopes aroused by such efforts were deferred from month to month. In the closing paragraph of the *Survey* for 1931-32, written just after the conclusion of the Lausanne Conference, attention was drawn to the "note of cautious optimism sounded by the first reactions of the stock exchanges" to the hopes of political settlement and economic reconstruction raised by the agreement reached at Lausanne. It is a delicate and, indeed, an impossible task to ascertain the exact weight of political considerations in such a complex economic situation; but there is almost universal agreement that the prospect of political settlement was a factor, equally with the hope of economic reconstruction, in the return of business confidence that marked the second half of 1932.

That it was not the only factor goes almost without saying. Whatever the original causes of the depression may have been, the economic wreckage that had piled up during its continuance called for very comprehensive technical adjustments, and a large measure of reconstruction. The mere fact that the average level of prices had fallen in less than three years by something like 40 per cent meant that virtually all contractual relationships were thrown out of equitable and effective adjustment. The delicate balance between wages, the cost of living, and wholesale prices, for example, was destroyed, so that wages, even when reduced, might still be too high when viewed as costs of production in relation to wholesale prices, but might, on the other hand, be low in relation to the cost of living. The real burden of debt charges had been enormously aggravated, fixed monetary incomes had increased in real value, but profits and variable incomes had generally shrunk. Within national economies, and internationally, the long-continued economic depression had disrupted the accepted scale of values and thrown all sorts of relationships into confusion.

There were some grounds for believing that, at the low point

of the depression reached in the summer of 1932, such technical economic adjustments as the equation of costs to prices had progressed considerably in certain countries and in certain industries. In so far as such adjustments had actually taken place, the way had been cleared for the normal economic stimuli to bring about a measure of recovery. Though subsequent developments, particularly in the United States, caused serious doubts as to the adequacy of liquidation at that time, it was widely believed in the late summer of 1932 that recovery was imminent and speculative anticipation of such a recovery was a major factor in the "boomlet" which raised security prices substantially in the autumn.

The analysis of the economic situation in the summer of 1932, which was made in a preceding section, however, suggests that, in addition to further domestic adjustments in many countries, important measures of reconstruction, adequate to restore the international economic co-operation that had broken down so badly, were essential before any recovery could be solid. No measures of economic adjustment within the power of individuals or commercial groups could restore lasting vitality to a world in which the international monetary system was destroyed, international trade had been pinched to a fraction of its former value and the whole international financial system was in disarray. To remedy such a fundamental breakdown, action by responsible Governments was clearly necessary.

Before such action could be taken, however, there were outstanding political conflicts, misunderstandings and mistrusts to be cleared up. The business world was beginning to realise that trade was not likely to expand until the restrictions upon it were removed, that the establishment of a stable monetary standard demanded close and continuous international co-operation, that the hope of prices rising, of credits being "unfrozen", of "blocked" accounts being transferred, depended largely upon the Governments concerned coming to a series of satisfactory agreements upon these complex problems. But it did not require much political knowledge or imagination to realise that the prospects of securing such close technical collaboration upon vital economic problems depended largely upon a prior solution of certain outstanding issues of a more political character. In many of these political issues there were important economic elements. This was the case, for instance, with reparation payments and war debts. The economic aspect of disarmament was clearly important also, not only because of the magnitude of the expenditures involved, but also because the allied problem of security entered largely into the economic nationalism which was expressed in tariff warfare and unwillingness to risk undue

economic or financial dependence upon the goodwill of other peoples. But, apart altogether from the economic aspects of such important political issues, the prospects of intimate and long-continued international collaboration in the difficult and harassing tasks of economic reconstruction would, it was recognised, be greatly enhanced by a lessening of political tension and mistrust. The political settlement of 1924-25 had been a prelude to increased economic activity, and, in the summer of 1932, great expectations were fixed upon the Lausanne Conference in the hope that it might settle some of the outstanding political problems that were dividing Governments, and commence, or at least clear the way for, the tasks of reconstruction.

The economic results of the Lausanne Conference were important, therefore, in three respects. In the first place, the mere fact of agreement upon some of the most vexatious issues that had embittered post-war European politics led in itself to a lessening of the political tension that had seemed to inhibit international co-operation. The hope revived that a better understanding among the principal European Powers would lead to further progress in such matters as disarmament and the organisation of peace and security, which in turn would make international economic co-operation more feasible.

The second achievement at Lausanne lay in the tentative agreement on a final solution of the reparation problem and the hope that this agreement would facilitate impending discussions concerning war-debt payments. The economic and psychological effects of these inter-governmental financial obligations had loomed very large in the depression, and many authorities had come to regard them as among the most important contributing causes, if not the original cause, of the breakdown of international economic and financial co-operation. Although the suspension of such payments under the Hoover moratorium of June 1931 had removed the actual economic burden during the twelve months in which the moratorium was operative, the psychological effect of maintaining the obligations, and the prospect of payments being resumed while economic activity, and particularly international trade, was at such a low ebb, remained as difficult obstacles to recovery. The agreement announced at the opening of the Conference prolonging the moratorium, as far as reparation payments were concerned, brought a considerable measure of relief. The subsequent agreement provided for the elimination of future payments in return for the delivery by the German Government to the Bank for International Settlements of 5 per cent redeemable bonds to the amount of three milliard Reichsmarks gold. These bonds are to be held by the Bank and are not to be negotiated before July 9th, 1935. After that date, the

Bank will negotiate the bonds by means of public issues on the markets as and when possible, in such amounts as it thinks fit, provided that no issue shall be made at a rate below 90 per cent. Any bonds not negotiated by July 9th, 1947, will be cancelled. The proceeds of the issues are to be placed to a special account, the allocation of which among the creditor Governments will be decided by further agreement among them in due course.

This settlement was conditional upon ratification by the Powers concerned, and such ratification, it was evident, would depend partly upon the progress made in subsequent discussions concerning the war debts. The very existence of such a conditional agreement was, however, interpreted as a considerable step towards the final elimination of both these disturbing financial legacies of the war.

The third way in which the Lausanne Conference broke new ground was by the preliminary steps taken to organise international action directed towards economic reconstruction.

By Section IV of the Final Act of the Conference it was decided to set up a committee "with the duty of submitting to the Commission of Enquiry for European Union at its next session proposals as to measures required for the restoration of the countries of Central and Eastern Europe". The following section of the Final Act invited the League of Nations to convoke a "Conference on Monetary and Economic Questions".

The Committee which came to be known as the "Stresa Conference for the Economic Restoration of Central and Eastern Europe" was constituted by delegates from fifteen European Governments.¹ Its terms of reference, laid down at Lausanne, concerned two broad problems :

(a) Measures to overcome the present transfer difficulties of the Central and Eastern European countries and to make possible the progressive suppression, subject to the necessary safeguards, of the existing systems of exchange control ; and

(b) Measures to revive the activity of trade, both among those countries themselves and between them and other States, and to overcome the difficulties caused to the agricultural countries of Central and Eastern Europe by the low price of cereals, it being understood that the rights of third countries "remain reserved".

¹ Austria, Belgium, the United Kingdom, Bulgaria, Czechoslovakia, France, Germany, Greece, Hungary, Italy, Netherlands, Poland, Roumania, Switzerland and Yugoslavia. The representative of Latvia was admitted to the Conference as an observer.

Quite clearly, these terms of reference, while of paramount importance to the countries immediately concerned, touched at more than one point the interests of many countries outside Central and Eastern Europe. The regional problems of Central and Eastern Europe could be profitably considered only in the setting of a world economy. The Commission of Enquiry for European Union received the report of the Stresa deliberations at its meeting in September 1932 and appointed a sub-committee to elaborate further the proposal made for a Currency Normalisation Fund, but deferred any action concerning the recommendations pending the Monetary and Economic Conference.

Another conference of great international importance was held in the summer of 1932 at Ottawa. Representatives of the United Kingdom and the self-governing dominions of the British Commonwealth, and India, together with the Secretary of State for the Colonies, negotiated a series of agreements designed to increase inter-Imperial trade. In one respect the discussions at Ottawa bore vitally upon the problems involved in any international action aiming at economic reconstruction. It was publicly stated by the leader of the delegation from the United Kingdom that the aim of his Government was to begin at Ottawa, and within the family circle of the British Commonwealth, a movement towards freer trade which might be carried further along a wider international front in subsequent negotiations at the Monetary and Economic Conference. The extent to which the agreements reached at Ottawa did in fact make for freer trade is examined in a later chapter. From the point of view of their effect upon the public estimation, in non-British as well as British countries, of the possibilities of immediate international action aiming at economic reconstruction, the conflicting reports while negotiations were proceeding at Ottawa, unavoidable delay in publishing the detailed schedules of the new duties, and the controversy that arose concerning their probable economic effects, all contributed to more sober expectations and therefore to an abatement of the optimism which had been aroused by the success at Lausanne. The guarded nature of the report upon currency policy and its references to the need for international, as distinct from imperial, agreement pointed also to a postponement rather than an acceleration of decisive action.

In the last quarter of 1932, therefore, the hope of rapid action to follow up and implement the agreement at Lausanne, and to build upon it a substantial measure of international co-operation in economic reconstruction, had been considerably discounted. Slow progress, or renewed tension, in the concurrent political discussions concerning disarmament and the Sino-

Japanese dispute contributed also to an abatement of the optimism expressed earlier in the autumn.

As the year 1932 drew to a close, the controversy that developed concerning the payment of the war-debt instalments due on December 15th still further clouded the horizon. The initiative in raising this problem was taken by the United Kingdom, whose instalment was by far the largest. In a brief note delivered shortly after the result of the Presidential election had been declared, a request was made, pending negotiations concerning a reduction of the debts, for an extension of the Hoover moratorium, which had expired since the previous payment. In the negotiations which followed, and notably in the second British note of December 1st, the ratification of the Lausanne agreement concerning reparation payments was linked with the possibility of war debts being treated similarly. The other European countries from which instalments were due opened up negotiations with the United States Government also ; but the latter stood firm in its request for payment. In the event, the United Kingdom, Italy, Czechoslovakia, Finland, Greece, Latvia, Lithuania, Roumania and Yugoslavia paid their instalments ; while France, Poland, Belgium, Estonia and Hungary did not. The British payment amounting to \$95,500,000 was made by earmarking gold to that value in the vaults of the Bank of England.

There were many other discouraging factors in the international situation, when the Preparatory Commission of Experts appointed to draw up the agenda of the Monetary and Economic Conference met in November 1932 and again in January 1933. Prices were falling again, optimism had been replaced by pessimism on the stock exchanges, unemployment was increasing and international economic equilibrium had been further disturbed by the fall in the exchange value of sterling which persisted through the late autumn and early winter.

The analysis of the economic problems confronting the world which the Preparatory Commission made for the Monetary and Economic Conference referred in its introduction to "certain auguries of improvement". These, it is evident from the context, were the signs of revival "after Lausanne" and particularly the fact that "more favourable monetary conditions, technical economic readjustments and reviving confidence are being currently interpreted by those who assume the risks of investment as affording the possibility of a genuine change for the better in the economic situation". This statement, written in mid-January, is, however, placed between two significant warnings. After summarising "the extremities to which the forces of disintegration have already carried the economic world" and stating that "further losses of ground cannot be

contemplated without the gravest forebodings", the experts concluded their introduction by a very emphatic denunciation of the prevailing economic warfare, and an equally emphatic warning to the Governments that "this prevailing conflict of national economies must be resolved" if "a full and durable recovery is to be effected". Before this warning could take effect, however, there were, within a month, a recrudescence of banking difficulties in the United States; an aggravation of the Far-Eastern dispute, leading to sharp falls in both Chinese and Japanese bonds; further depreciation of the currency in New Zealand and Denmark, and a marked decline in German bonds, in addition to such general developments as further declines in prices, production, employment and international trade.

The key to the economic situation, it was evident to the experts, was a restoration of international economic co-operation; but it is a difficult key to turn and becomes more difficult with delay. Moreover, a growing body of opinion in almost every country tends to become impatient and even intolerant of the seemingly futile efforts to find a solution by international action. Impressed by the clamant need for action in some direction, and by the evident possibility of immediate, if partial and often exaggerated, results from re-organisation within national or group boundaries, such opinion, which claims to be practical in contrast with the theories of international co-operation, tends to be reinforced by the vested interests which grow up behind currency or trade restrictions. The strong development of such autarchic doctrines was to be noted in many widely separated and diverse countries. The forms which this development took were as diverse as the countries where they appeared. Not the least significant from a long-run point of view was the increased pace of industrial development in hitherto backward industrial countries.

It is all the more significant, therefore, that the trend of expert opinion, as the depression deepened, became more and more definite and emphatic that a return to freer international economic co-operation was the true direction in which a solution might ultimately be found. The hardening of expert opinion along these lines may readily be traced, not only in the various reports and manifestos of committees of economists such as the League's Gold Delegation, and of such bodies as the International Chamber of Commerce and the International Chamber of Shipping, but also in the resolutions of the Board of the Bank for International Settlements and most clearly of all in the draft annotated agenda prepared for the Monetary and Economic Conference. The introduction to the draft agenda, indeed, declared specifically

that the alternative of national self-sufficiency "would shake the whole system of international finance to its foundations, standards of living would be lowered and the social system as we know it could hardly survive".

The positive plan of action envisaged by the Preparatory Commission in its draft agenda consisted essentially of a modest, but difficult, programme aiming at the restoration of international economic co-operation in four main fields—monetary and credit policy, price stabilisation, the restoration of capital movements and the progressive removal of trade restrictions. The technical details of this programme are best treated in their proper context in later chapters. At this point, however, the fact should be emphasised that there was a growing realisation in 1932 and early 1933 that national, imperial and regional schemes for economic reconstruction must be fitted into wider international programmes.

One of the first and most significant statements on this point is that contained in the report on currency policy drawn up by the financial experts at the British Imperial Conference held at Ottawa in July and August. This report, while laying down broad principles to be followed by the monetary authorities of the British Empire, contained the clear statement that such principles were conditioned and limited by the possibility of securing international co-operation in their application.

The conference at Stresa, with its proposals for economic and financial action to relieve the situation of the Central and Eastern European countries, developed in much the same way into regional preparation for the Monetary and Economic Conference.

The programme for the Monetary and Economic Conference set forth by the Preparatory Commission of Experts was the culmination therefore of much planning on more restricted lines. It incorporated also the main results of prolonged investigation and discussion by international economic and financial institutions, and, in particular, followed closely upon the principles contained in the report of the Gold Delegation of the League of Nations which had subsequently been endorsed by the Board of the Bank for International Settlements. It was based, therefore, upon a wide and developing body of expert opinion.

It is obvious that a programme consisting essentially of the reparation of mechanisms for international co-operation that had broken down under unprecedented strain did not contain any very revolutionary proposals involving departures from established practice. Panaceas holding the promise of rapid amelioration of existing conditions were conspicuously absent. There was no plan for world inflation, for work-spreading or

work-creation, and little encouragement to the advocates of world-planning. Rather there was a minimum programme of reconstruction to get the mechanism working again, together with proposals for clearing away the debris of past failures, and for cutting loose the restrictions that have impeded the mechanism. Emergency measures were suggested as necessary in certain special cases and some permanent improvements were outlined; but the programme as a whole was one designed to get the former international system working again rather than to construct an ideal new system.

The Preparatory Commission drafted its suggested agenda in the middle of January 1933; but in the interval between that time and the opening of the Monetary and Economic Conference on June 12th, a succession of important political and economic events changed the setting of the Conference very considerably. The banking crisis in the United States was followed by the abandonment of the gold standard and the passing of legislation which gave unprecedented powers to the President to take action in the monetary and economic field. The Conference opened, therefore, with the dollar added to the list of fluctuating paper currencies. A brief summary of the progress made in the early sessions of the Conference is contained in the last chapter of this *Survey*, but a fuller analysis must be reserved for later volumes.

Chapter II.

THE CONFUSION OF PRICES.

THE GENERAL TREND OF PRICES IN 1932-33.

Some indication was given in the *Survey* for 1931-32 of the background of instability which lay behind the collapse of the general price-level from 1929 onwards. It is not intended here to repeat or amplify that discussion, or to enter into the controversy concerning the causes of the price decline. There is general agreement that the causes are many and complex. Important and far-reaching changes in the geographical and technical structure of industry and trade; equally important social developments such as a rising standard of living together with lessened flexibility of adjustment; political difficulties arising from reparation and war-debt payments, and tariff wars; monetary problems connected with the post-war currency stabilisations and the working of the new gold standard after it had been restored; international capital movements, security speculation and exchange difficulties — all entered into the background of the price-fall. The exact degree to which these various factors entered into the combination of causes which precipitated the depression has been, and still is, a subject of lively controversy. In the pages which follow, however, no attempt will be made to discuss these causes. Attention will be directed rather to the various aspects of price-movements since the beginning of 1932.

The present section is devoted to an exposition of the general trend of prices in 1932 and the first quarter of 1933. The abandonment of the gold standard by the United States of America in April created an entirely different situation, which must be left for treatment in a later chapter. The discussion which follows treats of events to the end of March 1933.

Wholesale Price Indices of Certain Countries.

(Base: 1913 or 1914 = 100.)

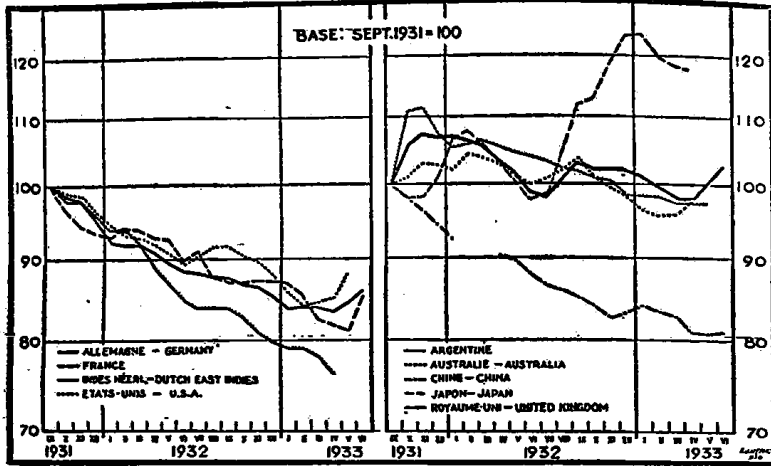
Country	Peak in 1929	March 1933	Date of the lowest point	Percentage decline from peak to	
				The lowest point	March 1933
Belgium	869.0	504.0	III/33	42.0	42.0
Dutch East Indies	150.0	77.0	III/33	48.7	48.7
France	660.0	390.0	III/33	40.9	40.9
Italy	499.0	287.0	III/33	42.5	42.5
Netherlands	147.0	72.0	III/33	51.0	51.0
Poland ¹	99.0	57.9	XII/32	43.2	41.5
Switzerland	142.9	90.0	IV/33	37.0	37.0
United States of America	138.2	86.2	II/33	38.0	37.6
Austria	135.0	107.0	I/31	22.2	20.7
Czechoslovakia	964.0	647.0	III/33	32.9	32.9
Estonia	123.0	80.0	III/33	35.0	35.0
Germany	139.6	91.1	I/33	34.8	34.7
Hungary	136.0	82.0	XII/32	40.4	39.7
Latvia	127.3	83.8	XII/31	36.5	34.2
Argentina	129.8	113.0	III/33	12.9	12.9
Australia	170.8	122.5	II/33	28.5	28.3
Canada	153.3	100.6	II/33	35.2	34.4
Chile	198.8	343.4	X/31	28.4	(+72.7)
Denmark	159.0	123.0	IX/31	31.4	22.6
Egypt	125.0	70.0	III/33	44.0	44.0
Finland ²	100.0	89.0	IX/31	21.0	11.0
Greece	1,854.0	2,017.0	VIII/31	23.6	(+ 8.8)
India	149.0	83.0	III/33	44.3	44.3
Japan	172.2	134.0	VI/32	35.8	22.2
Norway	167.0	121.0	IX/31	29.9	27.5
New Zealand	148.3	129.6	I/33	15.6	12.6
Peru	189.0	174.0	IV/32	13.8	7.9
South Africa	119.6	90.0	X/32	27.3	24.8
Spain	174.0	168.0	VI/30	4.6	3.4
United Kingdom ³	140.3	97.6	III/33	30.4	30.4
Yugoslavia ³	107.0	67.0	IX/32	42.2	37.4
China ²	107.4	107.1	I/29	5.3	0.3

¹ Base: 1927 = 100.

² Base: 1926 = 100.

³ Board of Trade Index.

Price Movements in Certain Countries — September 1931 to June 1933.



The continuing downward drift of the price-level in nearly all countries is very clear. There were few, on or off the gold standard, where the index-number for March 1933 did not stand at the lowest level yet recorded in the depression. In the United Kingdom the recovery after June-July 1932, though subsequently diminished by a falling tendency from October onwards, had not been wholly lost by March. In Chile and Japan prices rose substantially because of currency inflation. There was, in March, a slight upward movement in several countries coincident with the security speculation and exchange disturbances which were caused by the depreciation of the United States dollar. The full effect of this latter movement, however, cannot be estimated as yet, since it is not possible at the moment to foresee the developments of American monetary policy.

Apart from the unsettlement in March 1933, therefore, there had been only one period in the last four years during which the downward trend of prices had definitely been arrested. That period was for three or four months before and after the Lausanne Conference in July 1932. The average level of wholesale prices rose between June and October by a little over 2 per cent in the United States of America, and by almost 9 per cent in the United Kingdom, but, in many countries, the decline continued steadily, and in none, except where there was definite inflation, was the improvement anything but hesitating and temporary.

Continued political, economic and monetary uncertainty, the multiplication of trade restrictions, and renewed exchange fluctuations were the main factors in causing a reversion to deflationary tendencies in the winter of 1932-33. At the time of writing, at the beginning of May 1933, with the opening of the Monetary and Economic Conference still six weeks ahead, and national monetary policies still uncertain in most of the important financial countries, it is impossible to guess at the importance or probable duration of such rises of prices as occurred during March and April.

While the downward trend of prices had been practically universal and continuous from the beginning of the depression late in 1929 until February 1933, there was considerable variation in the extent to which the average level of wholesale prices, as measured in national currencies, had declined in particular countries. It is clear that prices fell most in those countries which retained a free gold standard. In those which interposed a buffer between world prices and prices in their domestic markets by allowing their exchange to depreciate, the extent of the decline was much less. It is significant, however, that in all cases, except those where currency inflation was resorted to, prices continued to decline after the first adjustments had been made to the new paper standards. In all cases too, except inflationary countries, prices stood at lower levels in March 1933 than before the abandonment of the gold standard.

The significance of these facts warrants more extended investigation than can be made in this *Survey*. It appears evident that, even without a common international standard of value, and in face of greater restrictions on the circulation of capital and the interchange of commodities than had previously been known, the price-systems of the various countries remained closely linked. Even though the units of measurement were different and world markets were broken, the general drift of prices was the same practically everywhere. How far this similarity of movement is inherent in the price-system or how far it was caused by policies and economic forces which were approximately the same in the main gold and non-gold countries is a question that lies outside the scope of the present discussion. The important fact to record here is that a mere change from the gold standard to a managed paper standard was not in itself sufficient in the given circumstances to affect any decisive alteration in the movement of prices. After a period of confusion during which there was some rise of paper prices to compensate for the exchange depreciation after gold had been abandoned as the standard, the movement of average prices, in default of positive inflationary

action, followed in every case the same general course as in the countries still adhering to gold.

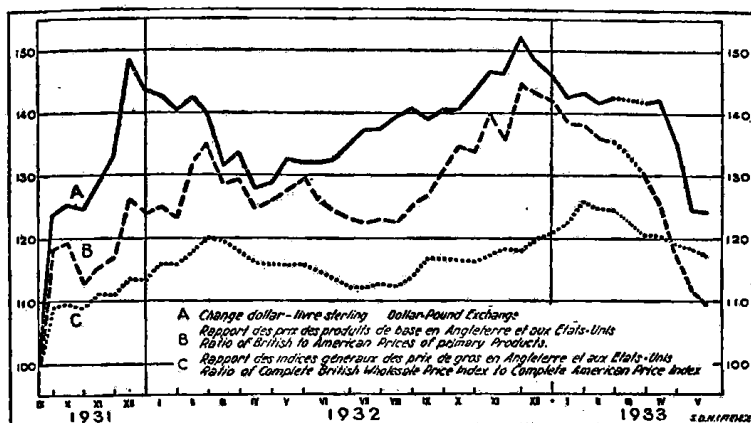
It should be added, moreover, that up till March 1933 the net effect of abandoning the gold standard had been to depress rather than raise gold prices. In a perfectly free economy, the lessened demand for gold might have been expected to lower its value and cause prices to rise. But, on the contrary, the demand for gold did not lessen. The increasing gold production of the world, supplemented by large amounts released from hoards in India and China, was readily absorbed at higher prices in terms of the managed currencies and in terms of commodities. The gold-standard countries, and many countries which had abandoned that standard, continued to buy gold as their resources permitted, and, in addition, a large demand for private hoarding sprang up in Europe and North America as currency instability became more widespread.

The depressing influence on commodity prices thus created was reinforced by a great variety of economic factors. As will be shown later, little progress was made in correcting many of the fundamental maladjustments of the price-structure. Production therefore continued to decline and prices to fall. In order to compete more effectively in world markets, the countries with managed currencies endeavoured to restrain any tendency for their domestic prices, and therefore their domestic costs, to rise, preferring to allow their exchange-rates to fall. Since many of these countries have very great influence in world markets, the lower levels of their export prices and the failure of their domestic prices to rise tended to depress world prices in general. Moreover, the countries remaining on gold attempted to meet the new competition from depreciated currencies by further deflation and also by increased trade restrictions, and in the latter they were joined by many of the countries off gold. The total effect of currency instability therefore was still further to depress the average level of world-prices.

The complex influences of short-term capital movements and psychological as well as economic factors rendered it difficult to reconcile the internal and external purchasing-power of many of the most important managed paper currencies during this period. Sterling, for example, depreciated in terms of gold currencies much more than sterling prices varied from gold prices. The fact that so many important currencies were fluctuating made any attempt to determine their true or "natural" ratios still more difficult. "Relativity" of standards became a problem of vital practical economic interest and importance, all the more because experience proved once again that currency

instability in itself (as distinct from conscious management) was a disturbing and depressing influence upon price-levels and economic organisation.

*Ratio of British and American Prices
and Dollar-Pound Exchange, 1931-1933.*
(Base: September 18th, 1931 = 100.)



The situation in March 1933, therefore, was not reassuring as far as the general drift of prices was concerned, and was equally disturbing when the continued and even aggravated price disequilibria, international and industrial, were taken into consideration. The actual extent to which wholesale commodity prices fell from the peak levels of 1929 varied considerably from country to country, but averaged about 40 per cent in terms of gold currencies. There were many individual commodities and large groups of products which fell more heavily. The raw materials and agricultural products which enter largely into international trade, for example, fell on the average about 50 per cent.

More significant in many ways than the extent of the decline has been its duration. The sharp fall of wholesale commodity prices in the crisis of 1920-1922 was greater in most countries than the more protracted fall in the present depression. Thus, in the United States in the years 1920-1922, prices fell for twenty-one months consecutively, the total fall being 45 per cent. In the years 1929-1933, on the other hand, prices fell 38 per cent ; but the fall was spread over 44 months, to February 1933, with only one brief period of respite.

While the fall in 1920-1922 was greater than it had become by February 1933, the circumstances of the two crises were very different. The fall in 1920 came after a very rapid rise of 140 per cent in the preceding five years (including a rise of 25 per cent in the final inflationary year), whereas the fall in 1929 followed a period of years in which commodity prices had been relatively stable with, on the average, a slight falling tendency. The adjustments in 1920-1922 were less difficult because there was less general expectation of maintaining the war and immediate post-war price-levels. In the present depression, the price-fall threw into confusion a much greater, and what had been regarded as a much more stable, complex of economic contracts and arrangements. The prolonged duration of the price-fall and the greatly increased resistance to the liquidation which was its natural consequence were indicative of a far more serious economic crisis during the past four years. So many expositions of the consequences of falling prices in the present depression are available that it would be superfluous to add another here.

Mention should be made, however, of another important if obvious fact. This is the second great depression within ten years and to some extent its effects are cumulative upon those of the first. In so far as liquidation was ineffective or incomplete after 1920-1922, the economic organisation was more vulnerable in 1929. This was particularly important in respect of the great volume of indebtedness in the world, which was incompletely written down in the previous crisis and subsequently was largely increased. Perhaps the most dramatic illustration of the cumulative aspect of the present price-fall is by a comparison with pre-war price-levels. The very drastic fall in 1920-1922 brought average wholesale prices — for example, in the United States of America — back to about the level of 1917, which was still 40 per cent above that of 1913. The subsequent drift downward, followed by the sharp fall after 1929, brought price-levels in most countries well below the pre-war standards — at the beginning of 1933, the level was 13 per cent in the United States, and in France, Italy and some other countries 18 to 19 per cent, below that of 1913.

THE PROBLEM OF INTERNATIONAL EQUILIBRIUM.

In the foregoing discussion, attention was paid solely to movements, in one country or another, of the average level of wholesale commodity prices as measured by well-known and accepted index-numbers. Such movements are the simplest, and, in many respects, the most important, price phenomena; but they ignore, and to some extent conceal, the significance

of the complex and confusing individual and group movements from which the average is compiled by a somewhat artificial calculation. The index-numbers that measure movements in the average or general level of wholesale prices tend, indeed, to focus attention, not upon the factors which influence prices from the side of the commodities exchanged, but rather upon the monetary factors which affect the standard of value. The chief use of index-numbers of wholesale prices has been to afford a rough measure of changes in the purchasing-power of the currency used as a standard of value. It has often been assumed that movements of individual prices about the average are in the main self-corrective and, for the purposes of monetary theory, comparatively unimportant. It has always been clear that violent movements of the average level, precipitated usually by fluctuations of the monetary standard in which all prices are measured, inevitably throw the prices of individual commodities out of adjustment and thus create disequilibria which have a disturbing effect upon production and trade. Recent experience, however, has emphasised the fact that there is a reciprocal effect of such disequilibria upon the movements of the average level. It is probable that divergent movements of commodity prices within the general average caused primarily by non-monetary factors, such, for example, as a bountiful harvest or new mineral discoveries, cheapening important raw materials relatively to finished products, may provoke changes in production and consumption which are sufficient in themselves to impart an upward or downward movement of the average price-level. It is true that the corrective processes which are immediately set up within the price-structure are generally powerful enough to prevent such an impulse from developing very far. As long as the price-system is reasonably flexible, the ready adjustment of price relationships to changed conditions in the demand and supply of particular commodities keeps the average level of prices on an even keel. In the absence of such flexibility, these non-monetary factors may be quite capable of causing a prolonged and persistent movement of the average, independently of, and even in opposition to, changes in the supply of monetary means of payment.

Such a situation seems to have arisen in recent months, when the price disparities described in the next section, between the prices of producers' and consumers' goods, and between those of agricultural and manufactured commodities in particular, proved obstinately resistant. The paralysis of production and trade, and therefore of consumption, that was the result of such maladjustments and of the devices introduced to prevent their removal by the harsher processes of competition was in itself

sufficient to force a continued price decline, even in face of an abundance of monetary means of payment.

If consideration is given, not only to wholesale commodity prices, but to the many other elements of the price-system — retail commodity prices for example, and all the complex relations that exist between various kinds of commodity prices and wages, interest rates, business profits, investment values, debt-burdens and taxation — the possibility of such a deadlock arising becomes still more obvious. Retail prices are more sluggish than wholesale, wage rates lag behind the cost of living, long-term contracts inhibit rapid changes in interest rates, the burdens of debt and taxation cannot readily be reduced as prices fall. If the elasticity of other parts of the price-system proves inadequate to absorb the shock which the original impetus to lower prices — however caused — imparted to the average level, the whole system may be tumbled into a confusion which itself becomes a further depressing influence. Once the elasticity of adjustment is broken in this way, the falling price tendency, opening out new and wider disequilibria as it progresses, tends to become self-perpetuating until no choice is left between an abandonment of the hindrances erected to competition or the application of some unorthodox device to break through the vicious circle.

The events of recent months, moreover, demonstrated the importance of a further disturbing factor in the price situation. The national currency systems based upon the gold standard, in which price-movements were formerly measured, was replaced by a confusion of standards so that the measurement and interpretation of price-movements, by practical traders as well as by economic theorists, became more difficult. To the disequilibria within national price-systems there was added a series of international disequilibria between these systems. The breakdown of the international gold standard was a result rather than a cause of such disequilibria, but it tended, like the maladjustments of commodity prices, to intensify and prolong the evils by which it was caused.

The disorganising effect of such developments is only too obvious. As long as there existed an international standard of value by reference to which temporary disequilibria could readily be gauged, international capital movements and commodity trade, influenced by and reacting upon interest rates and price-levels, were effective instruments by which equilibrium could be restored. In recent months the accepted international standard was replaced by a great number of competing and fluctuating standards. It is doubtful whether such confusion ever before existed, even in the inflation period immediately

after the war. For a time after the United Kingdom abandoned the gold standard in September 1931, there was discussion of sterling as an alternative standard to gold. The later tendency for the so-called "sterling bloc" to disintegrate as one country after another lapsed into further depreciation, followed by the appearance of the "managed" dollar as a further alternative, opened up a vista of fluctuating and competing standards which threatened the loss of any certainty yet remaining in international economic relations. As currencies shifted in relation to one another, it was not only the exporters, competing in neutral markets, who were affected, but the whole community. Price-levels and the relations between different sorts of prices, interest and capital obligations generally, wages and all economic contracts were altered by changing the standard in which they were valued. Depreciation in the external value of a currency was an aid to exporters, only so long as it was not followed by similar depreciation of other currencies. The advantages gained temporarily by depreciation were at the expense of competitors and ceased when depreciation became generalised.

Exchange depreciation, moreover, brought export advantages only when it kept ahead both of its international competitors and also of rising costs at home. Therefore, to the natural lag of domestic prices there was added a strong inducement for the countries which had abandoned gold to pursue monetary policies calculated to restrain any tendency for their costs of production to be increased. The counterpart of monetary nationalism was domestic deflation.

Recent experience has amply demonstrated this fact. Those countries which, for various reasons, found it necessary to abandon the gold standard, for the most part left their exchange free to find its own level, but pursued policies of internal price deflation in the sense of holding down costs of production as far as possible. This was a powerful factor in checking any possibility of prices rising. Moreover, export competition from countries with depreciated currencies was met by increased trade restrictions which put still further pressure upon the prices of those commodities entering into international trade. The narrowing of world trade and the disorganisation of production caused thereby was a major factor in forcing prices in general down to lower levels in recent months.

When the United States of America, by imposing an embargo on the export of gold on April 19th, definitely allowed the external value of the dollar to depreciate, this action was accompanied by the announcement of a monetary programme designed to give power to the Executive to proceed at its discretion with various types of monetary inflation. The legislative

measures embodying this programme have not been finally passed at the moment of writing and there is no certain indication of the extent to which action will be taken in pursuance of the authority granted to the President. A marked rise of commodity and security prices took place immediately, partly as a speculative anticipation of some form of monetary inflation. By the end of April, this rising tendency had spread to other countries and was still proceeding rapidly in the United States. The probable duration and influence of such a movement, however, remained incalculable if only because the consequences of any monetary programme that may be decided upon will be so largely dependent upon the extent to which it can be made international by agreements arrived at during the course of the Monetary and Economic Conference. Further consideration of the recent rise in prices must therefore be deferred.

It is evident, however, that a rising price-level is sought, not as an end in itself, but as a practical means of remedying the price disequilibria which at present block the way to recovery. The lesson taught by the experience of recent years, and of recent months in particular, is that, among those disequilibria, the disorganised relations between national price-systems as a whole take an important place. The following section sets out various anomalies in the relationship between the prices of different sorts of commodities, some of which have fallen more drastically than others. If an upward movement of prices is to take place, it is essential for sound recovery that these anomalies shall be removed as the average level rises, or, in other words, that the commodities which are at present unduly depressed shall rise faster than those whose prices have been relatively well sustained. The prices of agricultural raw materials imported into industrial countries, for example, should rise faster than the prices of manufactured commodities exported from those countries.

It is equally necessary that a workable equilibrium should be restored between the average price-levels in the various countries. Not only should the right prices rise, but they should rise in the right places. Fortunately, the two factors largely work together. A rising tendency of raw-material, and especially agricultural, prices in the great industrial countries would go far towards righting the balances of payments and improving the purchasing power of the agricultural and debtor countries. But the mere statement of such a fact is sufficient to show that monetary policies designed to produce such a rising price tendency are intertwined with and dependent upon all the other factors which enter into the balancing of international payments. The freeing of commodity trade, resumption of capital movements, debt settlements and restoration of an

international standard of value must be taken into consideration along with other measures of monetary policy designed, in raising prices, to remove price disequilibria.

THE DISRUPTION OF PRICE EQUILIBRIA.

It is a truism that, in a changing world, the prices of individual commodities and services are constantly shifting in relation to each other and to the average price-level. Prices are the indicators which register and, to some extent influence, changes, not only in trade, but in the whole organisation of economic life. Under the system of free enterprise, this flexibility of individual prices is the necessary condition of healthy growth and adaptation to changing circumstances. There is a constant flux of shifting relationships, not only between different sorts of prices recording transactions at different stages of the economic process, but also between individual commodities and groups of commodities, and between national price-systems as a whole. In periods of relative economic tranquillity, however, the changes, while incessant and rapid, are not great and are quickly neutralised or offset. National price-systems, especially when they are connected with an international monetary system, are kept in equilibrium by the smooth working of the foreign exchanges; movements of individual commodity prices cause compensatory adjustments in production and demand, not only for the particular commodity, but for all its related by-products, substitutes, and complementary commodities; while divergences between wholesale and retail prices bring similar competitive forces into play. The range of fluctuation therefore is narrow and movements of the average price-levels are comparatively slow and smooth.

Violent fluctuations of individual prices, reflected in sharp movements of the average levels, however they may be caused, are indicative of abnormal and unhealthy economic conditions. Beyond a certain limit, such fluctuations are apt to defeat the corrective forces that are adequate to check and reverse them in more normal times. When, for any reason, the price of a commodity like wheat takes such a headlong plunge as occurred in the first year of the depression, it is not possible for increased demand, decreased production, and adjustment of other commodity prices quickly to restore the broken equilibrium. Since a whole range of important commodities was affected in the same way at the same time, it was inevitable that business activity in general should be affected by such a disruption of equilibria. As the depression deepened, the disequilibria became more serious and extended their range. The relations between

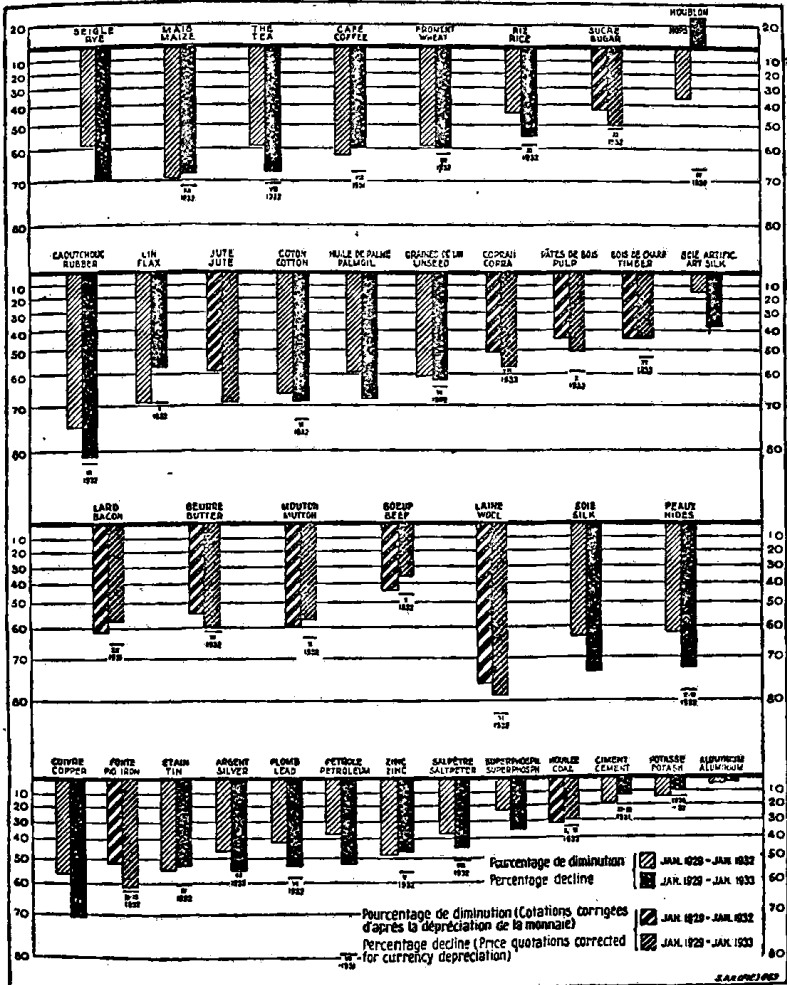
national price-systems became strained and the international monetary system broke down. As the confusion of prices increased, trade and industry became increasingly difficult, until it became generally recognised that the central point of the whole deadlock lay in the disjointed relations of various sorts of prices.

The *Survey* for 1931-32 described some of the most important price disequilibria created by the depression. It was there shown that the prices of individual commodities had fallen very unevenly, that growing disparities had developed between wholesale and retail prices in almost every country, and that there were important discrepancies also between the movements of significant groups of commodities. In the pages which follow, it will be shown that, up to the end of March 1933, these various disequilibria, so far from being remedied, had been aggravated. They had indeed become self-perpetuating in the sense that they blocked the recovery of economic activity and thereby tended to force prices lower. The following discussion follows much the same arrangement as that in the preceding *Survey*, and the statistical illustrations there given are brought up to date as far as possible.

THE COURSE OF INDIVIDUAL COMMODITY PRICES.

The series of diagrams on which are plotted the prices of several important foodstuffs and raw materials show that, for the great majority of these commodities, the price-fall at least slackened in the latter half of 1932. At the beginning of 1933, it is true, most prices stood at lower levels than they had reached a year earlier, but, in the great majority of cases, there had been some measure of recovery from the lowest points reached at various times during the year 1932. Such recovery as had occurred in the second half of 1932, however, was greatly diminished by the falling tendency of prices in the last quarter of that year and the first months of 1933, so that, by March, the net gain in most cases was not great. The average level of prices, indeed, was drifting lower.

*Percentage Change in Gold Prices
of Certain Foodstuffs and Raw Materials on World Markets,
January 1929 to January 1933.*



The lowest prices up to March 1933 were reached for the various commodities in the order recorded below :

1930 :	April :	Hops.
1931 :	July :	Petrol.
	October :	Coffee.
	December :	Bacon.
1932 :	January :	Flax.
	February :	Beef.
	April :	Tin.
	May :	Zinc.
	June :	Rubber, cotton, linseed, butter, wool, hides.
	July :	Timber, lead.
	August :	Tea, copra.
	October :	Wood pulp, mutton.
	November :	Rice, sugar, coal.
	December :	Maize, wheat, pig-iron, silver, cement.
1933 :	March :	Rye, jute, palm oil, artificial silk, silk, superphosphates.

It is evident from this tabulation that there was no uniformity in the movement of prices as far as these products were concerned. At the end of March, not only were several commodities at the lowest levels of the depression, but many others which had risen slightly in previous months from their lowest points were either falling again or were showing little movement. When all were combined in a weighted average, the movement was still downward.

In the first quarter of 1933, therefore, there was little real stabilisation or promise of the price-fall being reversed. The prices of most textiles were 60 to 80 per cent below the levels at the beginning of 1929; cereals and other foodstuffs were 50 to 70 per cent lower; animal foodstuffs, 40 to 60 per cent lower; most of the non-ferrous metals, including silver, were 50 to 55 per cent lower, though copper was down by more than 70 per cent; coal had fallen only about 35 per cent, and cement, potash and aluminium even less.

WHOLESALE AND RETAIL PRICES.

It is possible to group and contrast wholesale commodity price-movements in a variety of ways. It can be shown, for example, that raw materials fell more than manufactured goods, and goods used for immediate human consumption more than those used for capital equipment. Part of the explanation for the latter phenomenon can be demonstrated by showing how cartellised (monopolised) prices fell less than those of free goods. The

greater fall of raw materials and consumption goods clearly caused a price-fall of greater significance in those countries whose main products are agricultural, so that the terms of trade run against such countries as their exports fall more heavily than their imports. There were, it is obvious, many factors at work in causing such discordant price movements; but the greatest and most important was to be found in the weak bargaining position of the agricultural producers. The major disequilibrium of prices throughout the depression was caused by this weakness and there was little sign up till March 1933 that it was being removed.

In passing, it may be pointed out that the heavier fall of wholesale than of retail prices was partly due also to this phenomenon. Index-numbers designed to measure retail prices or the cost of living include a wide range of manufactured articles and even services. Rent, lighting, transport and a whole wide range of miscellaneous personal expenditure, as well as finished articles of food and clothing, are included in such calculations. There are many fixed or semi-fixed prices, such as rent charges fixed by contract for a term of years, or conventional standardised prices — for example, tramway and railway fares — in retail-price indexes, whereas index-numbers of wholesale prices include mainly competitive commodity prices.

It is not surprising therefore to find that the cost-of-living or retail-price indices fell much less than the indices of wholesale prices, especially when it is remembered that retail trade is more localised and less competitive than the great speculative world-markets in which wholesale prices are mainly determined.

Percentage Decline in Wholesale and Retail Prices in Certain Countries from the Average Levels ruling in 1929 until March 1933.

Country	Wholesale prices	Retail prices
Belgium	40.8	16.8
Canada	32.6	21.3
Denmark	18.0	9.2
France	37.8	5.9
Germany	33.6	24.2
India	41.1	32.2
Italy	37.0	17.3
Japan	19.3	20.5
Netherlands	49.3	17.9
Sweden	25.0	10.0
Switzerland	36.3	18.0
United Kingdom	28.5	16.5
United States of America	36.8	28.2

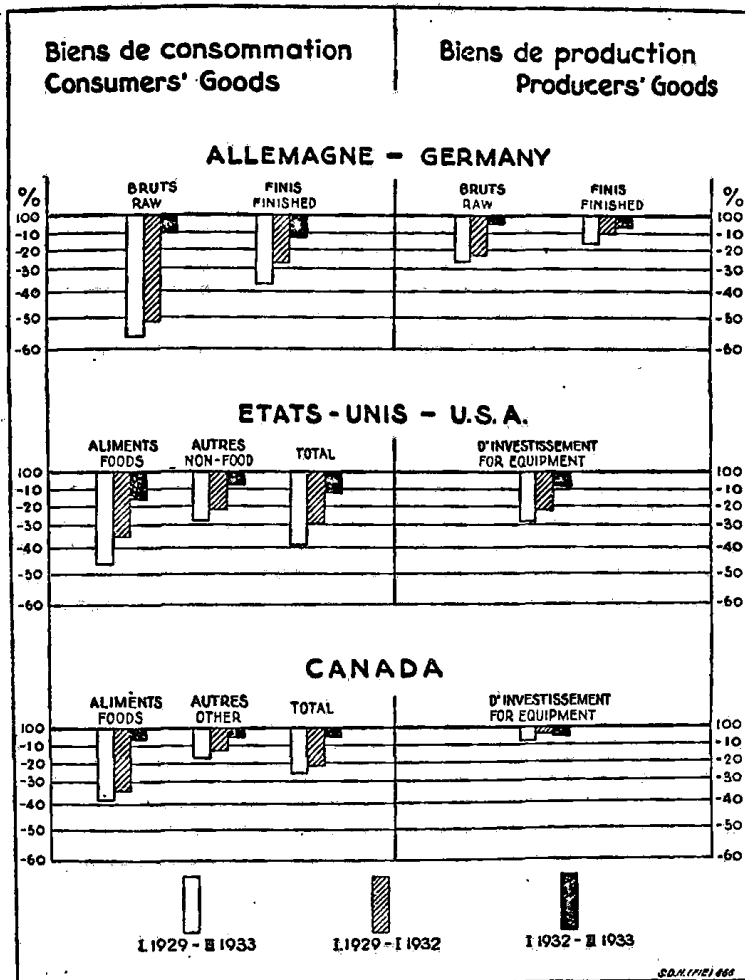
Such divergences of movement, however, did not represent a widening of the differences between the prices of commodities at different stages of manufacture so much as variant movements of the prices of different commodities and services. If wholesale and retail prices of the same commodities are compared, the differences are much less important. Thus, from the beginning of 1929 to March 1933, the wholesale and retail prices of foodstuffs fell in the percentages shown below :

Country	Wholesale	Retail
British India	38	33
Canada	45	38
France	30	6
Peru	17	12
Switzerland	33	26
United Kingdom	32	28
United States of America	45	39

THE COLLAPSE OF AGRICULTURAL PRICES.

It will be shown in the next chapter that agricultural production, the world over, has been sustained in a remarkable degree. The reasons for this are obvious enough and have often been set forth. The cruel paradox by which the world has witnessed the piling up of large stocks of foodstuffs and raw materials, while agricultural prices fell to ruinous levels and widespread unemployment checked demand, was largely a price phenomenon, or, in other words, a problem of disordered exchange. The marked discrepancy between agricultural prices and those of manufactured goods, evident even before the depression set in at the close of 1929, continued and was even aggravated in 1932-33. In March 1933, the disparity was wider than ever and in its train there followed a shrinkage of purchasing power which crippled manufacturing production, a tightening of the international financial position of the agricultural debtor countries, continued difficulty in reconciling the prices of consumers' and producers' goods and almost insuperable obstacles to the re-starting of industrial, trade and investment activity.

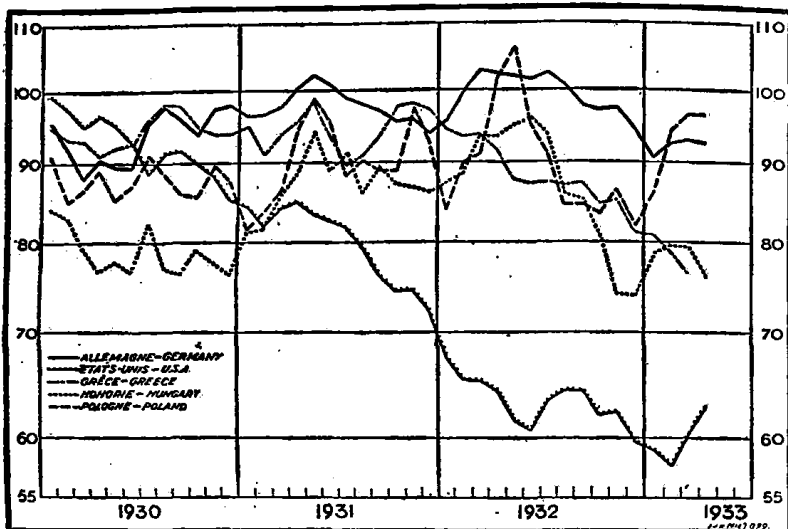
Price Indices of Producers' and Consumers' Goods.



In face of the sharp decline of agricultural prices on world markets, there was a growing tendency to protection in those countries where the agricultural industries depend primarily upon the domestic market. This protection, expressed not only by higher tariffs, but also by the imposition of the various forms

Price Indices of Agricultural and Industrial Goods : Agricultural Goods as a Percentage of Industrial Goods¹.

(Base : 1929 = 100.)



of quantitative import restriction described in a later chapter, cut off the markets of the world one from another. The following table will show the marked difference between the course of agricultural prices in the exporting countries and in those where agriculture is largely a domestic industry.

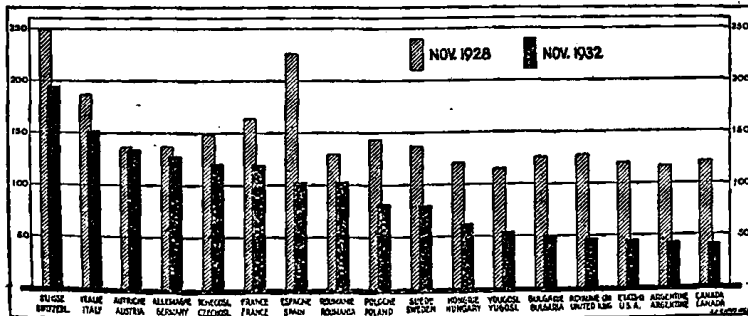
¹ Germany : Indices of "Agricultural Products" and "Industrial Products".
United States : Indices of "Farm Products" and "Non-Agricultural Commodities".
Greece : Indices of "Agricultural Products and Industrial and Chemical Products".
Hungary : Indices of "Agricultural and Breeding" and of "Other Industries".
Poland : Indices of "Agricultural Products" and "Industrial Products".

*Percentage Decline in Agricultural Prices of Certain Countries :
January 1929 to March 1933.*

Country	Decline in national currency	Decline in gold prices
Argentina	51.4	70.5
Australia	35.9	65.5
Austria ¹	15.3	27.1
Canada	53.2	61.0
Dutch East Indies ¹	40.7	40.7
France	30.4	30.4
Germany	37.4	37.4
Greece	7.4	59.4
Hungary	45.4	45.4
India ¹	38.3	56.4
Italy	46.0	47.2
New Zealand ¹	11.5	50.1
Switzerland ¹	33.1	33.1
United Kingdom ¹	32.1	52.1
United States of America	59.6	59.6

The decline of prices in the exporting countries, measured in gold, was from 60 to 70 per cent. In those countries which normally import at least part of their agricultural requirements, special measures were taken to maintain domestic prices at a relatively high level. As one illustration of the extent to which the world market was broken into several non-competing markets there may be shown the following diagram of wheat prices, originally prepared for the Preparatory Commission of Experts which drew up the draft annotated agenda for the Monetary and Economic Conference.

Wheat Prices (in Terms of Gold) in Certain Importing and Exporting Countries, in November 1928 and November 1932. (U.S.A. cents per bushel.)



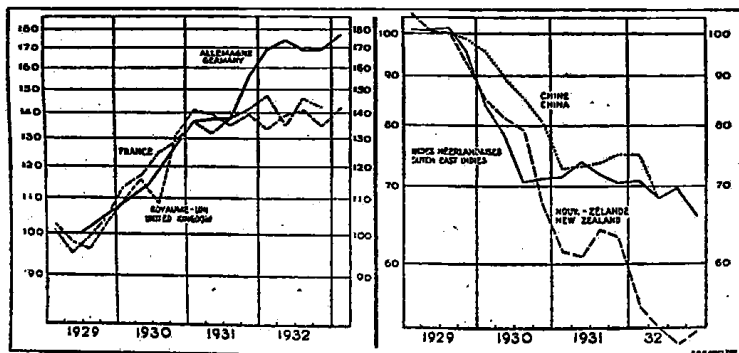
¹ Foodstuffs only.

Wheat is not the only example that might be given. Thus from the end of 1929 to the end of 1932, the world-market (Rotterdam) price of rye fell by 59 per cent; but in Germany the fall was only 10 per cent, in Czechoslovakia 16 per cent and in Sweden 33 per cent. In Denmark, the price of butter fell by 64 per cent; but in France the fall was 27 per cent, in Germany 36 per cent, and in Italy 40 per cent. Cuban sugar, free of duty, fell in New York by 58 per cent and other qualities fell on the world market in similar proportion; but in Germany sugar prices rose 20 per cent, in Poland they fell 12 per cent, and in New York, duty paid, they fell 25 per cent.

The fall in agricultural prices, moreover, was not accompanied by a comparable reduction in the costs of agricultural production. Many of these costs are fixed by contract over a long term of years. In a time of depression, interest upon mortgage indebtedness, railway freights, overdraft charges for current expenses do not fall quickly. Labour costs fall more slowly than prices, and the prices paid for materials are maintained at higher levels than those which the farmer must accept for his produce. It has already been shown that, on the average, agricultural prices in the exporting countries fell by 60 to 70 per cent. But, in the United States, non-agricultural products fell by only 32 per cent in the same period, and a selected list of commodities purchased by farmers declined even less.

*Export Prices as Percentage of Import Prices: Quarterly Movement
(Germany 1929 and 1930: Annual Movement).*

(Base: 1929 average = 100. Logarithmic scale.)



Note. — The left-hand curves (*i.e.*, those for Germany, France and the United Kingdom) show the prices of manufactured goods exported as percentage of those of raw materials imported.

It is obvious also that, with such a drastic fall of agricultural prices, the terms of trade ran heavily against the agricultural

debtor countries. Industrial communities found their import prices fall more than their export prices, while agricultural countries suffered the reverse movement. The situation thus created may be summarised briefly in the following table :

Import and Export Prices and Terms of Trade of Certain Countries, 1929-1932.
(Base: 1927 = 100.)

Country	Import prices				Export prices				Terms of trade (export price as percentage of import price)			
	1929	1930	1931	1932	1929	1930	1931	1932	1929	1930	1931	1932
France	94	80	65	55	96	92	77	65	102	116	118	118
Germany	101	88	68	50	97	93	82	71	97	106	120	141
Italy	90	78	61	48	85	71	58	49	94	91	95	103
Switzerland	97	87	75	64	102	96	86	76	106	110	115	119
United Kingdom	99	87	70	65	97	93	83	76	99	107	119	119
U. S. A.	92	75	57	42	101	91	72	62	110	122	126	146
Argentina	84	84	84	.	105	94	71	.	125	111	84	.
Australia ¹	90	90	82	.	97	77	57	.	108	86	70	.
Canada ²	95	84	71	.	95	77	64	.	100	92	90	.
Denmark	101	86	76	81	110	92	70	61	109	106	92	76
Dutch East Indies	97	91	72	59	77	52	36	28	79	57	51	47
Finland	97	79	67	81	97	91	74	73	101	115	110	91
India ²	94	77	65	.	91	72	60	.	97	94	93	.
Latvia	91	80	69	72	88	76	57	46	96	94	82	64
New Zealand	98	97	95	93	106	84	65	59	109	87	68	63

The other side of this story, of course, was the marked shrinkage of imports into the agricultural countries, which is demonstrated in a later chapter.

It is of some interest to note that the agricultural protection that was so greatly increased in the industrial countries contributed directly to worsening this situation. The purchasing power of the agricultural exporting countries was in any case much reduced ; but the prices at which the industrial countries could export to them were maintained at high levels because the cost of living did not fall as quickly as it might have done with freer trade. This is clearly shown in the following table :

¹ Years ending June 30th.
² Years beginning April 1st.

*Percentage Decline in Retail Prices of Foodstuffs
1929-1932 (Annual Averages).*

Countries exporting foodstuffs		Countries importing foodstuffs	
	Per cent		Per cent
Dutch East Indies	52	Italy	22
Bulgaria	39	Switzerland	19
Canada	37	Sweden	17
U.S.A.	35	France	14

OBSTACLES TO INDUSTRIAL RECOVERY.

In the preceding discussion, stress has been laid rather upon the disruption of international equilibrium occasioned by the disproportionate fall of agricultural prices. The importance of this aspect of the question is very great, both in itself and as leading to the measures of tariff protection, currency depreciation, and other forms of interference with international commerce that so greatly complicated and aggravated the depression.

The international disequilibrium thus caused was, however, not the only untoward consequence of the uneven price-fall. There developed a series of discrepancies between the prices of important commodity groups, which blocked the restoration of industrial production. In the groupings which follow, it will be clear that there is some measure of similarity, produced largely by the fact that the discrepancy between agricultural and industrial prices, though not the only influence at work, was the most important. Thus it was the low and uncontrolled prices of agricultural commodities that largely accounted for the discrepancy between the prices of raw materials and those of finished products, and between the prices of consumers' goods and those of investment goods. In the same way, agricultural commodities weigh heavily among the non-cartellised as opposed to the cartellised commodities. Since the prices of agricultural products continued to fall on the average in 1932 at least as fast as those of manufactured products, it is not surprising to find that the "scissors" movements in the price-structure, so far from closing, tended to widen in the last year.

In the *Survey* for 1931-32, a table was given showing the percentage fall in the wholesale prices of raw materials and manufactured goods in four countries for which indices were available. For comparison this table is now brought up to date.

Percentage Fall in Wholesale Prices of Raw Materials and Manufactured Goods.

Country	January 1929-January 1932		January 1929-January 1933	
	Raw materials	Manu- factures	Raw materials	Manu- factures
Canada	38	22	46	27
Germany	31	21	35	29
Italy	44	30	49	33
United States	41	25	49	31

It will be clear from this table that, only in Germany, where there was, during the first half of 1932, a marked deflation of prices affecting particularly cartellised goods, was there any closing of the gap. The principal reasons for the widening of this gap were obviously those which further depressed agricultural prices during 1932. The stoppage of capital imports and the necessity of repayment, throwing an extremely heavy strain on the agricultural debtor countries, the very disorganised state of world markets, the piling up of surpluses as import restrictions narrowed the area of international trade, and the many hindrances to a reduction of manufacturing costs and prices placed the producers of raw materials in an unenviable position. It should be stressed that the defences erected by the importing countries against the competition of low-priced agricultural products, by concentrating the surplus exports still more heavily in the remaining markets, contributed to aggravating the price-fall and therefore the disequilibrium between raw materials and finished products.

The variant movements of cartellised and non-cartellised prices may be used to illustrate one factor which partially explains the more resistant prices of manufactured goods. It was much easier to fix prices and control production for a fairly limited range of manufactured articles than it proved to exercise control over the scattered production of agricultural commodities. It can be shown that mineral raw materials, as a group, fell in price less than those of vegetable or animal origin. This was largely due to the greater ease with which mineral supplies could be controlled; and, in many cases, the control of production was reinforced by producers' agreements which were sometimes international in scope and capable of controlling prices in world markets. Monopoly of varying degrees of completeness and permanence is found in many forms over a great part of the

industrial system, but is much less evident in agriculture. Its effects are difficult to measure, but the German indices of cartellised and non-cartellised prices throw some light on the extent to which it is responsible for the present price discrepancies.

Cartellised and Non-cartellised Prices in Germany, 1929-1933.
(Base: 1926 = 100.)

January	Cartellised	Non-cartellised
1929	104.6	101.9
1930	105.0	90.4
1931	95.2	66.2
1932	84.3	51.2
1933	83.5	45.7

In Germany, it should be remembered, strong pressure was brought to bear upon the cartels by the Government. The Fourth Emergency Decree of December 1931, for example, stipulated that the prices of cartellised products should immediately be reduced to a level at least 10 per cent below that prevailing in June 1931. In these circumstances, the magnitude of the discrepancy between the price-movements so far recorded is significant of the important influence exerted by monopolistic controls.

Finally, attention may be drawn again to the important discrepancy which continued to widen between the price-movements of consumer's goods on the one hand and those of investment or producers' goods on the other. The significance of this problem was pointed out in the preceding *Survey*. The relatively high prices of the commodities required for industrial construction and equipment in comparison with those paid by the final consumers constitutes an important impediment to recovery. During 1932, the discrepancy was widened rather than narrowed.

Comparable indices are not available for many countries, but they all point in the same direction. In the United States of America, the index-numbers prepared by the National Bureau of Economic Research show that the price of capital goods fell by 27 per cent up to the end of 1932, while consumers' goods fell 37 per cent. In other countries, the situation was worse. In Germany, producers' goods had fallen only by 16 per cent, while consumers' goods fell 35 per cent. In Canada, producers' equipment fell only 7 per cent and consumers' goods 26 per cent.

The relatively high price of investment goods as compared with the prices of finished products available for immediate consumption goes far to explain the failure of low-interest rates

and abundance of monetary resources to stimulate a revival of investment. Capital was available, but there was little opportunity of using it profitably. The materials used in the heavy industries — coal, iron and steel and building materials, for example — increasingly passed under the control of large concerns which followed policies of price stabilisation in good times and bad. Changes in demand were met by altering output rather than prices. But, in recent years, the fall in other commodity prices was so great that the gap which widened between the relatively stable prices of these producers' goods and the abnormally depressed prices of consumers' goods became an important hindrance to any prospect of recovery.

THE PRICE SITUATION IN MARCH 1933.

The facts set out in the preceding pages may perhaps best be summarised by comparing the fall in prices with a landslide which carried with it buildings, fields, walls and living objects. As the landslide continued, the more vulnerable of the buildings collapsed and, in collapsing, started a fresh downward movement. The difficulty of arresting the landslide and of shoring up or re-building the economic structure was at least greatly complicated by the confusion caused by the distorted relationships into which various sorts of prices fell.

The disequilibria which were created were of many kinds, industrial and international. Concerning the latter, little more need be added to the statement contained above of the dangers inherent in fluctuating and competing standards of value. The Gold Delegation stressed the importance of international economic co-operation in many diverse spheres of activity as a necessary condition of the re-creation and operation of an effective international monetary mechanism.¹ The events of recent months have shown the disturbing effects of currency instability to be so great that the converse proposition might now be defended, that it is essential to "re-create an effective international monetary mechanism" in order to secure a greater degree of willingness to co-operate in many other spheres of activity.

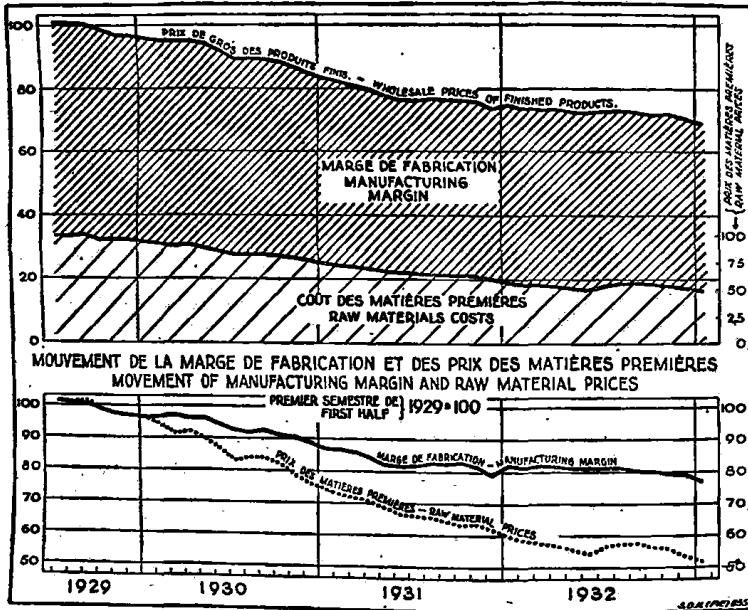
The necessity for remedying industrial price disequilibria and, in particular, for reducing the discrepancies set forth in the previous section, is also sufficiently obvious to be generally recognised, but it may be worth while to draw attention to the manner in which such disequilibria have actually blocked recovery and tended to become self-perpetuating.

¹ See report of the Gold Delegation, paragraphs 39 and 40.

The key to the problem lies in the existence of overhead costs, which are difficult to reduce as the prices of most commodities fall. It is possible to demonstrate the fact that, even after full allowance was made for the lower prices of raw materials, the manufacturing profit-margin in 1932 was still reduced by comparison with 1929, because overhead costs were spread over a smaller production. There was definitely a vicious circle, in which lowered demand consequent upon falling prices of raw materials and upon wage reductions, diminished output, smaller gross profits and still lower raw-material prices and wage-payments followed in unbroken succession.

The diagram which follows, reproduced from the chapter on prices in "World Production and Prices, 1925-1932",¹ compares the fall in the prices of finished products with that of raw-material prices. On the assumption that in the first half of 1929 the cost of raw materials represented on the average a third of the final cost of the finished product, the price-curve for raw materials

*Raw-Material Costs, Finished Product Prices
and the Manufacturing Margin in the United States of America.
(First half 1929 = 100.)*



¹ Formerly the "Review of World Production". This chapter was circulated, as an advance print, to the Monetary and Economic Conference.

is plotted on a scale which is reduced to one-third. The gap between these two curves, plotted separately below, represents the gross profit margin of manufacturing, and this margin will be seen to have diminished.

Obviously this rather crude picture ought to be elaborated by a study of the movements of other costs of production — such, for example, as wage-payments. It is probable, indeed, that such studies occupy much of the attention of business organisers in many countries at the present time. There has been a substantial decline in other costs than those of raw materials. The cost of labour, for example, fell in the United States of America by about 25 per cent from 1929 to the beginning of 1933. Administrative and operative costs have also been lowered and some reduction has been made in capital costs, but resistance to liquidation has been particularly strong in this field. This is brought out by the following table :

*Changes in Selling Prices and Production Costs of Manufacturing Industries in the United States, 1927-1931.*¹
(Measurements relate to changes per unit of product.)

Year	Average selling price	Average cost of materials	Average cost of fabrication	Average labour cost	Average overhead cost, plus profits
1927	100	100	100	100	100
1929	98	95	102	93	108
1931	78	72	89	80	95

This slow reduction of the overhead unit costs of production contrasts with the much more effective liquidation carried through in the previous crisis from 1919-1921. The comparable figures may be summarised as follows :

	Percentage decline 1919-1921	Percentage decline 1929-1931
Average selling-price of manufactured goods	22	20
Average costs of manufacture, per unit of product :		
Materials	23	24
Fabrication	18	13
Labour	6	14
Overhead, plus profits	27	12

¹ National Bureau of Economic Research, *Bulletin*, No. 40. Frederick C. Mills : "Changes in Physical Production, Industrial Productivity and Manufacturing Costs".

It was the large volume of industrial debt that was contracted on the basis of a higher price-level in the years 1922-1929 that proved the most difficult obstacle in the way of adjusting the prices of finished products to those of raw materials. The burden of capital costs was difficult to reduce. Where, as in the cartellised industries producing investment goods, it proved possible to maintain prices, the resistance to liquidation of the capital structure was particularly strong. The dilemma thus created had not been solved at the beginning of 1933. A revival of investment and productivity was still checked by the relatively high prices of investment goods. Efforts to stimulate investment by the provision of abundant and cheap credit had proved ineffective and, in default of such stimulation, the prices of raw materials and foodstuffs lacked the support of effective demand.

Chapter III.

THE DISORGANISATION OF PRODUCTION.

STATISTICS OF WORLD PRODUCTION.

The previous chapter outlined some of the salient aspects of the confusion into which the price system has fallen during the depression and laid special stress upon the disruption of price equilibria, both international and industrial. Such substantial shifts in price relationships are of great importance in their effects upon the distribution of national incomes, altering the shares received by those — wage-earners, owners of capital, and producers of raw materials — who co-operate in the production of commodities and services. Even if no alteration in the available volume of goods and services had resulted, price changes would have brought about drastic readjustments in the distribution of income.

Since, however, productive organisation is, in fact, greatly influenced by the relative prices of different goods and services, account must be taken also of the disorganising effects of violent price fluctuations on production. There is, obviously, action and reaction between these phenomena, price changes being influenced by, and in turn causing changes in, the structure of production. In the *Survey* for 1931-32, which dealt largely with the background and early development of the crisis, the chapter on production was placed before that on prices in view of the importance attached to the rôle of structural changes in productive organisation in creating the conditions which were responsible for the fall in prices. A previous chapter, however, had been devoted to the part played in promoting such structural changes, and also in disturbing price equilibria more directly, by monetary policies in the period preceding the depression. It is always difficult to disentangle such complex factors as those which operate to create violent price fluctuations, and the order of priority decided upon in any discussion must

depend largely upon an estimate of the relative emphasis to be given one factor or another at any particular time. In the *Survey* for 1931-32, emphasis was laid upon structural changes in industry, caused in part by monetary policies, as an important factor among those responsible for the fall in prices ; but attention was called to the fact that the falling price-level and the disequilibria which emerged as prices fell were in turn exercising an important influence upon industrial organisation.

In the present *Survey*, the order of treatment has been reversed, prices being discussed before production, as an indication of changing emphasis at a different stage in the cycle. Stress is laid now rather upon the disturbing effects of the price disequilibria created as the general level of prices has fallen. It has already been shown that these disequilibria have caused a considerable diminution of production and have acted as blocks to any substantial recovery of industrial activity. The present chapter is mainly devoted to an examination of the statistics which measure the decline of production ; but in the course of that examination it becomes quite clear that the disorganised state of production is a cause as well as an effect of falling prices. It is this constant action and reaction of one set of phenomena upon the other that constitutes the main difficulty, not only of economic analysis, but also of practical action to remedy the depression. In more normal times, with a more flexible economy, corrective forces within the economic system were generally sufficient to readjust prices and production ; but, in a time like the present, when fluctuations have been exceptionally violent and when, moreover, rigid inflexibilities have appeared at various points in the economic organisation, the natural recuperative powers of free enterprise appear to be insufficient to restore balanced production and prices.

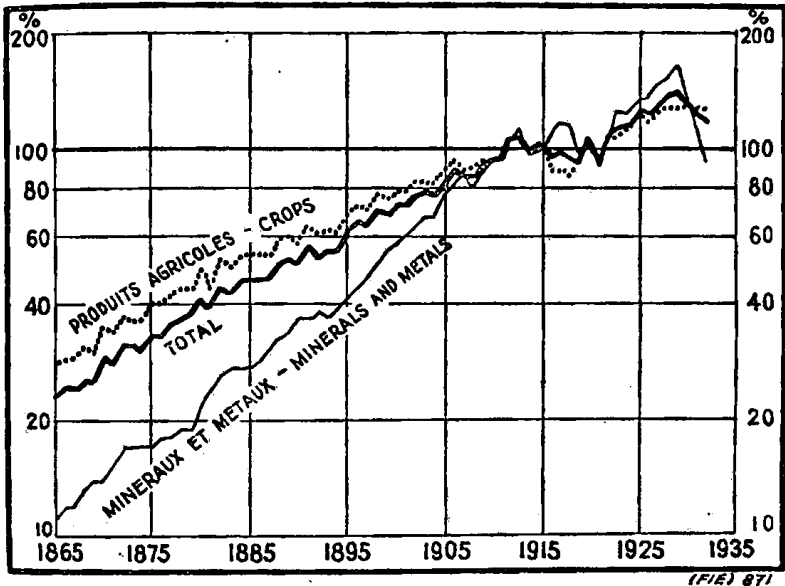
For many decades before the war, world production, according to the best estimates available, increased with remarkable regularity of trend, broken only in minor degree by successive crises. This trend of increase ran through both the period of declining prices from 1873 to 1895 and the period of rising prices from 1895 onwards. Most of the estimates available over such a long period measure the production of raw materials and foodstuffs. The index of world production calculated by the New York Federal Reserve Bank, for example, is compiled from the production statistics of important crops and mineral raw materials. The diagram reproduced on the following page, showing the results of these calculations, gives a clear picture of fairly regular increase till 1913-14, when a minor depression was turned into a definite decline in production during the war period. The post-war recovery appears from the diagram to have proceeded at a rather greater annual rate of increase,

starting, however, from a much lower level than might have been the case if the war had not interrupted the previous trend.

The statistical basis upon which such estimates rest is necessarily somewhat slender, and too much importance should not be attached either to the precise figures or to the exact rates of increase ; but there is no reason to believe they do not correctly indicate the general trend of development.

*Indices of Total World Production of Basic Commodities since 1865.*¹

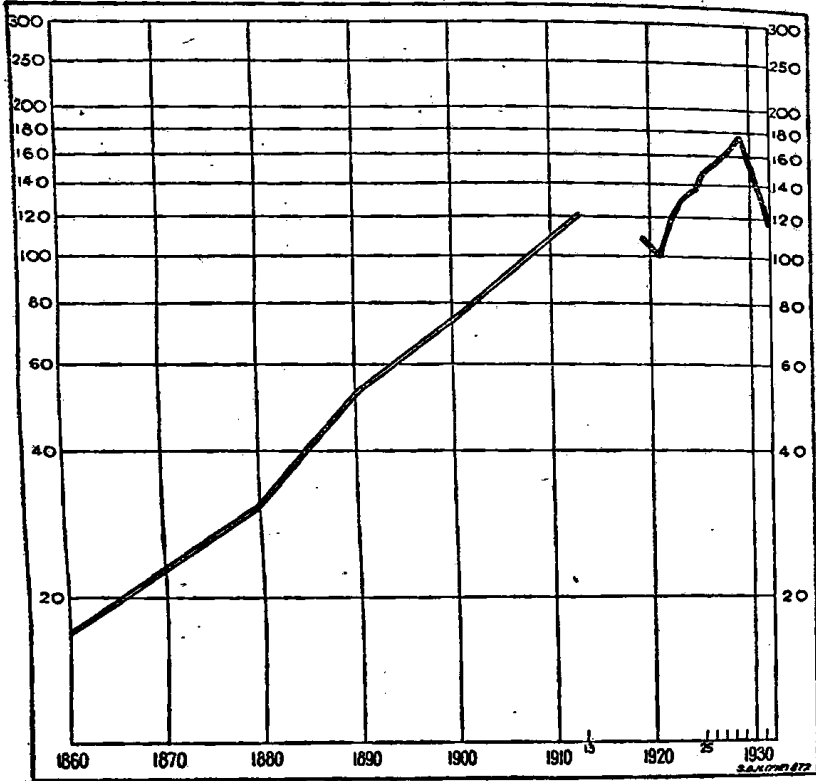
(Base: 1910-1915 = 100.)



If account be taken of the various forms of manufacturing activity, the available calculations indicate that the total of world production (as distinct from the production of raw materials and foodstuffs) in the pre-war period not only increased at a faster rate, but fluctuated more widely than the curves shown in this diagram. The rate of increase shown in the diagram which follows is much closer to that of minerals and metals than to that of crops in the preceding diagram, since manufacturing production undoubtedly increased much faster than population and the need for foodstuffs.

¹ Federal Reserve Bank of New York, *Monthly Review*, May 1933.

Index of World Industrial Production, 1860-1932.¹
(Base: 1901-1913 = 100.)



In the war period it is evident that the decline of production was caused more by declining food supplies, largely due to the reduction of production in Europe, than by the decline in mineral production, and it is probable that manufacturing production increased at that time even more than the production of raw materials would suggest. Even so, production as a whole was much below the levels that might have been expected if the pre-war trend had continued. The statistics of production, therefore, reveal the fact that the prosperity and economic activity of the war period were largely illusory. Monetary

¹ Institut für Konjunkturforschung — Sonderheft 31 — “Die Industriewirtschaft”. The index includes mainly mining, the heavy iron, textile and food industries.

inflation concealed the real diminution in wealth which was the result of the disturbance to productive organisation.

For the post-war period, and particularly the years of depression since 1929, the results obtained by the League's investigations confirm those obtained by the Federal Reserve Bank of New York and the German Institut für Konjunkturforschung. There has been, since 1929, a much greater decline in world production as a whole than any recorded in previous crises; that decline has been concentrated mainly in manufacturing production, which has suffered even more severely than the production of metals and minerals; agricultural production, on the other hand, "has shown nothing more than a halt in its upward trend". These facts appear clearly in the following table comparing various indices of world production.

Indices of World Industrial Production compared with Indices of World Production of Industrial Raw Materials and Foodstuffs.
(Base : 1925-1929 = 100.)

Index	1925	1929	1930	1931	1932
<i>Institut für Konjunkturforschung :</i>					
World industrial production (including U.S.S.R.)	92	111	100	90	77
World industrial production (excluding U.S.S.R.).	93	110	96	84	69
<i>League of Nations :</i>					
World production of industrial raw materials (including U.S.S.R.)	92	111	102	91	79
World production of industrial raw materials (excluding U.S.S.R.)	93	111	100	89	76
World production of foodstuffs (including U.S.S.R.)	98	103	103	102	103
World production of foodstuffs (excluding U.S.S.R.)	98	103	102	102	104
World production of all agricultural products (including U.S.S.R.)	98	104	103	103	102
World production of non-agricultural products (including U.S.S.R.)	90	114	101	86	73

It will be seen that two sets of indices are given, including and excluding the U.S.S.R. In order to bring out more clearly the importance of this distinction, it is perhaps necessary to

summarise the statistical information which is available concerning production in that country. The figures quoted below are derived from official statistics published by the Soviet Government.¹

The economic side of the Five-Year Plan for the reconstruction of agriculture and industry in Soviet Russia may be roughly summarised by describing the plan as an attempt, on the one hand, to re-organise agriculture upon a large-scale, collectivist basis, and, on the other hand, the rapid construction of the basic heavy industries — mineral production, transport, electric power, metallurgical and machine production — necessary to provide a foundation for the future extension of a wider range of manufacturing industry. The whole plan, drafted in great statistical detail, has been directed in accordance with centralised State policy. Monetary expansion has been accompanied by Government monopoly of foreign trade and the foreign exchanges, the external value of the rouble being maintained at gold parity, while its domestic value has depreciated. Despite rapidly increasing production of industrial raw materials and, to a less extent, of heavy manufactures, standards of living have remained low and have even decreased, the extra resources made available being utilised for capital construction. In fact, also, the equipment programme has been facilitated by long credit on the part of exporters in foreign countries,² and by the shipment abroad, particularly in 1930-31, of large quantities of foodstuffs and raw materials — for example, wheat, wood and petrol.

Difficulties of organisation in the later stages of the plan appear to have slowed up the rate of progress substantially. In such a vast scheme of reconstruction, the problem of maintaining an even pace of advance along a wide front was not a simple one. At times and in places transport was inadequate, raw materials short, essential machinery lacking, and, in consequence, the general rate of progress was slowed down and some confusion created. More definitely, in the last two years agricultural

¹ For critical estimates of these statistics cf., e.g., V. Timoshenko, "Agricultural Russia and the Wheat Problem", Stanford University, 1932; and *Wochenbericht des Instituts für Konjunkturforschung*, December 14th, 1932.

² The foreign debt of the U.S.S.R. was, according to an estimate of E. M. Shenkman in *Weltwirtschaftliches Archiv*, October 1932:

	Roubles (000,000's)
October 1929	415
October 1930	625
October 1931	855
June 1932	975

production has fallen and the lack of agricultural surpluses to exchange for further industrial equipment has reduced imports, besides still further lowering, in many regions very seriously, the already low standard of living. Agricultural production in 1932 was seriously deficient in many regions.

The Industrial Development of the U.S.S.R. ¹

	Unit	1928	1929	1930	1931	1932
Electrification :						
Generating capacity	Kw. (000's).	1,874	2,344	2,894	3,878	4,567
Production of electricity	Kw. hours (000,000's).	5,003	6,386	8,231	10,453	13,100
Industry :						
Gross production of census industries:						
Total	Milliard roubles at 1926-27 prices.	15.7	19.8	25.2	30.9	34.8
Producers' goods	"	7.0	9.0	12.7	16.0	18.0
Consumers' goods	"	8.7	10.8	12.5	14.9	16.8
Production :						
Coal and lignite	Tons (000,000's).	35.8	41.7	47.1	53.5	63.0
Raw oil	"	12.3	14.5	18.6	22.3	21.4
Pig-iron	"	3.3	4.3	5.0	4.9	6.2
Steel	"	4.2	4.9	5.8	5.3	5.9
Machines	Roubles (000,000's)	1,122	1,619	2,421	4,796	
Agricultural machinery	at 1926-27 prices.	—	270	453	731	890
Motor-cars	Number (000's).	0.9	1.5	8.5	20.5	...
Tractors	"	1.4	4.5	12.7	39.9	...
Cotton piece-goods	M. (000,000's).	2,871	3,068	2,161	2,087	
Woolen piece-goods	"	84	102	114	117	
Agriculture :						
Acreage	Ha. (000,000's).	113	118	122	136	134
Harvest :						
Wheat	Tons (000,000's).	21.9	18.9	26.9	...	...
Rye	"	19.3	20.3	23.6	...	...
Cotton	Tons (000's).	254	277	345	400	...
Transport :						
Railway freight traffic	Tons (000,000's).	88.1	112.9	133.9	145.4	188.8
Foreign Trade :						
Imports	Roubles (000,000's).	946	836	1,059	1,105	811
Exports	"	788	890	1,036	699	564
Monetary Conditions :						
Money in circulation	"	2,028	2,773	4,302	5,465	6,183

¹ League of Nations *Statistical Year-Book, 1932-33*. "Report of the State Planning Commission of the Council of People's Commissars of the U.S.S.R. Summary of the Fulfilment of the First Five-Year Plan", Moscow, 1933, also "Narodnoje Chasjajstwo".

On the industrial side, also, the attempt rapidly to develop capital equipment on a modern scale for a vast and increasing population has resulted in much the same phenomena of unbalanced production and over-capacity in the heavy industries as were the result of the investment boom in the rest of the world from 1925 to 1929. Russia's boom, different in management and policy, but essentially similar,¹ and even exaggerated in its economic development, continued till 1932; but in that year idle and unfinished plant betrayed the unbalancing of production. The special difficulties connected with the improvisation of a skilled labouring force and the co-ordination of industrial equipment have made the great effort at rapid capital construction much more costly than it might otherwise have been.

It is beyond the scope of this survey to attempt any estimate, if, indeed, such an estimate is yet possible, of the extent to which the difficulties both of agricultural and of industrial organisation are likely to prove permanent or destructive of the Soviet system. Nor will any attempt be made to estimate the probabilities of the increased industrial equipment being used in future, on the one hand, to meet the increased domestic demands which may arise because population increases or the low standard of living rises, or, on the other hand, to compete on world markets either in the east or in the west.

Finally, to summarise the geographical changes in the world production of foodstuffs and raw materials, the table given on page 90 of the *Survey* for 1931-32 is here brought up to date. It will be noticed that the provisional estimates for 1931 have been revised.

General Indices of World Production of Crude Foodstuffs and Industrial Raw Materials, weighted by 1930 Values.

(Base: 1925-1929 = 100.)

Continental groups	1925	1929	1930	1931	1932 [*]
Europe, excluding U.S.S.R.	95	112	103	99	99
Europe, including U.S.S.R.	94	111	105	102 [*]	101
North America	97	102	94	90	82
Latin America	95	104	104	99	90
Africa	95	109	107	103	102
Asia, excluding U.S.S.R.	97	104	109	103	101
Oceania	93	102	111	109	111
World	96	106	102	98	94

¹ Cf. J. Åkerman, "Det Ekonomiske Læget, 1932", Stockholm 1932.

^{*} Provisional.

It is of interest also to analyse in more detail the movements of production in recent months. As the following diagram shows, the lowest levels of production were reached in most countries in the third quarter of 1932. The substantial rise in most cases in the fourth quarter of the year, followed by a further fall in the first quarter of 1933, which, however, did not reach the low point of the depression, substantiates the outline of economic developments recorded in Chapter I. At the time of writing, in the first days of June 1933, there was a renewal of the upward trend of production in most countries.

THE MAINTENANCE OF AGRICULTURAL PRODUCTION.

The maintenance of agricultural production throughout the depression, despite the extraordinarily low levels of prices ruling for foodstuffs and raw materials, has given evidence of the marked stability and the fundamental importance of farming even in modern highly developed capitalistic economy. The provisional estimates now available for 1932 show that, in most parts of the world, and in the world as a whole, the production of foodstuffs increased as compared with 1931 and reached levels as high as or higher than those of 1929. This stabilised production, though in marked contrast with the decline in industrial production, yet falls below the levels which might have been reached if the pre-war trend, or even the trend from 1925-1929, had been continued, levels, it may be added, which are warranted by increasing population.

Indices of World Production of Crude Foodstuffs, weighted by 1930 Values.

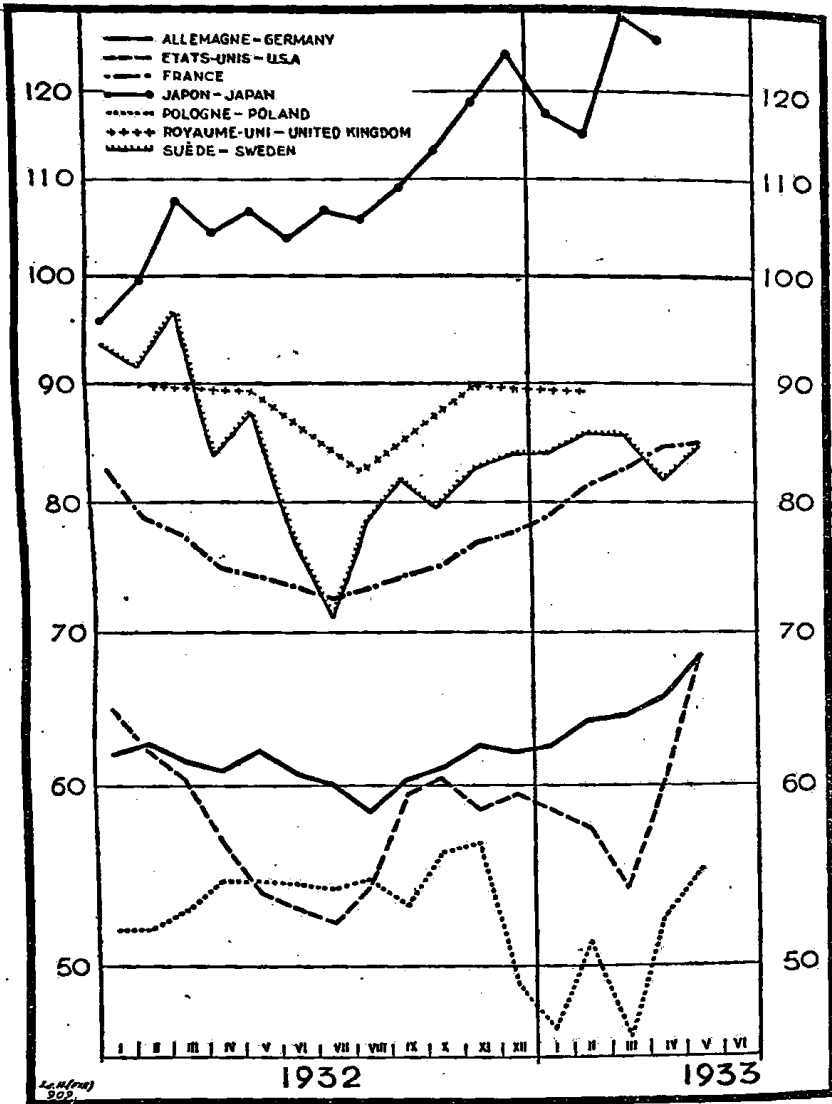
(Base : 1925-1929 = 100.)

Continental groups	1925	1929	1930	1931	1932 ¹
Europe, excluding U.S.S.R.	98	109	104	105	110
Europe, including U.S.S.R.	97	108	105	104 ¹	106
North America	99	96	94	97	101
Latin America	97	102	103	99	94
Africa	95	107	105	108	110
Asia, excluding U.S.S.R.	98	103	108	106	102
Oceania	93	102	119	116	118
World	98	103	103	102	103

¹ Provisional figures.

Monthly Indices of Industrial Production in Individual Countries to March 1933.

(Base: 1928 = 100)



Note. — Indices are adjusted for seasonal variations except in the case of France, Japan and the United Kingdom.

The production of agricultural raw materials has not been maintained quite so well, but throughout the world, except in Asia, has suffered much less than the production of non-agricultural raw materials.

*Indices of World Production of Agricultural Raw Materials,
weighted by 1930 Values.*
(Base : 1925-1929 = 100.)

Continental groups	1925	1929	1930	1931	1932 ¹
Europe, excluding U.S.S.R.	94	121	84	89	83
Europe, including U.S.S.R.	95	115	95	105 ¹	100
North America	104	100	98	113	86
Latin America	96	95	102	106	81
Africa	97	111	107	94	93
Asia, excluding U.S.S.R.	95	105	109	96	95
Oceania	91	104	102	108	110
World	97	105	103	103	93

These two tables, read together, indicate the influence of changes in relative prices of agricultural commodities. As will be shown later, the fall both in the production of industrial raw materials and in manufacturing production has been very severe.

The demand for agricultural raw materials such as textiles therefore fell heavily. The fall in demand also caused a sharp contraction of such agricultural products as rubber; but, in addition, there appears to have been a considerable shift from such commodities as textiles to the production of foodstuffs. This change-over has further been stimulated by policies of agricultural protection, which, as shown in the previous chapter, have in many countries maintained the prices of foodstuffs, and particularly cereals, at much higher levels than the prices either of foodstuffs or of agricultural raw materials in world markets. This fact is of some importance in considering whether there is, in reality, a general state of agricultural over-production in the world.

The group indices of production bear out the conclusion that the increase of agricultural production during 1932 was partly due to a shift from raw materials to foodstuffs. Such a shift is obviously not easy in many regions; but the marginal areas which can be used for different sorts of crops, or the breeding of animals for food rather than for raw material production, such as usually takes place in the later stages of a prolonged depression, are quite sufficient to bring substantial changes of production. It will be seen from the table below

that, while the production of cereals has increased by 4 per cent since 1929, the production of textiles has fallen by 10 per cent, that of rubber by 19 per cent, of vegetable-oil materials by 8 per cent and that of the tropical beverages — coffee, tea, cocoa — by 19 per cent.

*Group Indices of Production in the World as a Whole,
weighted by 1930 Values.¹*

(Base : 1925-1929 = 100.)

Groups of products	1925	1929	1930	1931	1932 ²
Cereals ³	100	100	102	100 ³	104
Cereals and other food crops ²	99	101	104	102 ³	104
Meat ¹	94 ³	105 ³	102 ³	103 ³	...
Wine and hops	109	107	92	99.	103
Coffee, tea, cocoa	88	120	94	110	103
Tobacco	99	107	111	109	...
Vegetable-oil materials	95	106	102	104	98
Textiles	96	106	103	105 ³	95
Rubber	79	132	126	122	107
Wood pulp	85	117	114	99	...
Fuels	93	110	102	92	84
Metals	88	116	95	71	51
Non-metallic minerals	87	112	107	93	77
Chemicals (fertilisers)	88	121	114	87	...
All agricultural products	98	104	103	103	102
Crude foodstuffs	98	103	102	102	103
Agricultural raw materials	97	105	103	103	93
Non-agricultural raw materials	90	114	101	86	73
All industrial raw materials	92	111	102	91	79
General index	96	106	102	98	94

The declines in rubber and in coffee, it may be added, are calculated from extraordinarily high peaks in 1929. Part of the investment boom in the years 1925-1929 was the undue stimulation of these tropical crops.

If the undue expansion of these tropical agricultural products during the boom is set aside as a special problem which the depression has already gone far to correct — as far as surplus production is concerned if not in regard to accumulated stocks — it is clear that it is difficult to uphold the view that there is any great amount of over-production of agricultural products at the present time. On the contrary, a comparatively slight

¹ League of Nations *World Production and Prices, 1925-1932.*

² Excluding China, except certain crops and meat in Manchuria.

³ Figures partly based on estimates or subject to revision.

change in demand might well reveal a problem of under-production and scarcity. Such a conclusion may appear paradoxical at a time when so much attention is centred upon the great accumulated stocks of agricultural foodstuffs and raw materials which overhang world markets. The experience of the last crisis (1920-21) is sufficient, however, to demonstrate how quickly very great accumulations of raw materials may be dissipated when trade is restored and demand revives.

The fact that there has been some change-over from the production of industrial raw materials to that of foodstuffs emphasises the possibility of accumulated stocks ceasing to be burdensome, if trade barriers are lowered and industrial production revives. An increase of 20 per cent in the activity of those industries which utilise textile raw materials, for example, would quickly alter the agricultural price situation in certain areas.

It is true that, in recent years, for social and political as well as economic reasons, agricultural protection in many countries, particularly the industrial countries of Western Europe, has grown to the point where, under present conditions, a problem of temporary over-production, at least of cereals, has been created. Before attempting to analyse the factors, in Europe and elsewhere, that have created this situation, the statistical position may perhaps be illustrated by the following table showing the production of wheat in various areas during recent years. This table should be read together with the price statistics given in the preceding chapter, not only for wheat, but for other cereal products.

*Wheat Production in Importing and Exporting Countries.*¹
(Quintals, 000,000's.)

Countries	1925-26 to 1929-30	1930-31	1931-32	1932-33
European importing countries	261	252	268	330
European exporting countries ²	104	119	123	74
Overseas exporting countries ³	463	469	444	433

¹ League of Nations *Statistical Year-Book*, 1932-33, *Bulletin Mensuel de Statistique Agricole et Commerciale*, International Institute of Agriculture, Rome, February 1933.

² Bulgaria, Hungary, Poland, Roumania, Yugoslavia.

³ Argentine, Australia, Canada, United States of America.

While these statistics must be interpreted cautiously in the light of harvest variations, they reveal the fact that the non-European exporting countries have at least maintained their production, despite an unfavourable harvest in the United States in 1932-33, at the same time as the European importing countries, aided it is true by good harvests in 1932-33, have greatly increased their production. The decline in the European exporting countries was largely caused by a poor harvest, and the elimination of the U.S.S.R. from the statistics does not greatly change the situation, since the production there seems to have fallen in 1932-33. Fuller details of the changes in acreage and yield are given in the table below :

*Area and Yield of Wheat Production in Certain Countries,
1929 to 1932.*

(Base : Average 1926-1930 = 100.)

Country	Area				Production			
	1929	1930	1931	1932	1929	1930	1931	1932
<i>European Importing Countries :</i>								
France	102.2	101.7	98.4	101.4	124.5	84.2	97.5	122.3
Germany	94.6	105.3	128.1	134.8	99.3	112.3	125.5	148.3
Italy	97.6	98.6	98.3	101.3	116.6	94.2	109.7	123.8
Spain	98.5	103.2	104.3	103.7	107.9	102.6	94.0	124.8
Switzerland	98.6	101.4	101.4	103.8	102.4	87.2	97.7	100.5
Sweden	105.5	119.1	125.5	137.2	111.0	121.6	105.4	150.8
United Kingdom .	90.9	92.2	82.1	88.1	100.1	85.0	76.1	87.7
<i>European Exporting Countries :</i>								
Hungary	93.8	105.9	101.4	98.6	91.4	102.8	88.4	71.4
Roumania	88.7	99.0	112.3	93.0	90.1	118.1	122.2	53.9
Yugoslavia	109.3	110.0	110.9	101.1	116.8	98.8	121.5	65.7
U.S.S.R.	98.7	108.1	123.7	115.4	82.6	117.7	...	...
<i>Non-European Exporting Countries :</i>								
Argentina	76.1	93.4	82.8	94.7	64.7	92.4	87.4	92.1
Australia	104.1	126.3	100.8	108.3	81.5	137.1	121.8	128.4
Canada	105.6	104.1	109.2	113.6	69.9	96.5	73.7	98.3
United States . . .	105.4	102.9	93.1	92.8	94.6	99.8	104.8	84.6
Total World Production¹	105.0	108.8	105.6	102.2	100.3	107.4	106.7	101.2

¹ Excluding U.S.S.R.

The increased production revealed in these tables must be considered in the light of the price movements discussed in Chapter II, the accumulation of stocks discussed in the following section of this chapter, the paralysis of capital movements discussed in Chapter X, and the increasing restrictions on international trade discussed in Chapter VIII. When all these factors are considered together, it becomes clear that such over-production as exists is not great relatively to world demand even at the present time and would be still less if consumption should appreciably revive in the near future. The problem is essentially one of restricted trade and broken markets — as such, it is sufficiently serious. The fact that in many European countries at the end of 1932 the domestic price of wheat was from three to four times as great as the domestic price in Canada is clear proof that the production in those countries is vulnerable and could not be maintained at its present levels except by costly subsidies. The situation has been reached, therefore, where many Governments are paying heavy subsidies to maintain production, which is sold at three times the price ruling in other countries where the Governments (as in the United States) are contemplating or actually administering restriction schemes which involve payments to farmers for not growing wheat.

While it is sufficiently clear that a lifting of trade barriers and a revival of consumption might quickly change the whole situation, the difficulties of removing the trade barriers should not be under-estimated. As long as prices remained at the low levels ruling in March 1933, the countries which had expanded their wheat production behind the shelter of tariff and other forms of protection were reluctant to invite the demoralisation of their farming industries by a removal of this shelter. They demanded that prices should rise, if necessary by prior action taken to control the marketing of stocks and to regulate production in the non-European exporting countries, before they could consider an abatement of their agricultural protection. Even if these conditions should be obtained, however, the social and political, as distinct from the economic, reasons for such protection would preclude drastic or hasty action.

THE DECLINE OF MANUFACTURING PRODUCTION.

In sharp contrast with the facts recorded in the preceding section, the production of industrial raw materials, and still more of manufactured products, has declined very substantially. After 1929, the decline accelerated from year to year; but the low point was reached in the third quarter of 1932 and there has

been some recovery, on balance, since then. The production of raw materials fell by slightly less than 10 per cent in 1930 from the 1929 levels; the fall from those levels was almost 20 per cent in 1931 and 30 per cent in 1932.

There is no precedent for such a marked decline. Statistical series ranging back to 1860 fail to reveal any previous period in which the decline in either raw-material production or manufactures has been so precipitate or so severe. Independent estimates agree that, in 1932, the level of industrial production in the world as a whole fell below that of 1913.¹

The damage wrought by the war and post-war disorganisation of industry may be estimated by comparing the actual position of production in 1932 with that which might have been reached if the pre-war trend of increase had continued. If the line of trend from 1860 to 1913 is extended to 1932, the rather startling conclusion is reached that the index of world production, on the hypothesis that nothing had occurred to alter its regular upward trend for the fifty preceding years, would to-day be rather more than twice as great as it actually is. While such a conclusion must remain highly speculative and hypothetical, it affords some measure of the cost to the world of the disturbances to productive organisation in the last twenty years. The existence of accumulated stocks of certain commodities and of over-capacity in some industries must be considered with the statistical evidence of greatly reduced production which follows.

*Index-Numbers of Industrial Raw Material Production, weighted by 1930 Values.*²
(Base : 1925-1929 = 100.)

Continental groups	1925	1929	1930	1931	1932 ³
Europe, excluding U.S.S.R.	90	117	102	90	80
Europe, including U.S.S.R.	89	117	106	97	90
North America	94	108	94	82	61
Latin America	91	111	107	98	77
Africa	95	112	109	95	90
Asia, excluding U.S.S.R.	93	107	111	99	98
Oceania	93	103	99	99	101
World	92	111	102	91	79

¹ Cf. the series quoted in the first section of this chapter — viz., those of the Economic Intelligence Service of the League of Nations and the German Institut für Konjunkturforschung.

² League of Nations, *World Production and Prices, 1925-1932*.

³ Provisional figures.

If attention is now turned to world industrial production, which includes mainly manufacturing and mining, it will be seen that there has been a decline of probably 37 per cent if the U.S.S.R. is excluded from consideration. This decline of 37 per cent is the estimate of the German Institut für Konjunkturforschung according to its index of world industrial production reproduced below. In the same table, the indices of industrial production of certain larger groups of countries are given.

International Indices of Industrial Production¹ and World Indices of Production of Industrial Raw Materials.²
(Base : 1925-1929 = 100.)

Nature of indices	1925	1926	1927	1928	1929	1930	1931	1932 ³
I. Indices of Industrial Production :								
A. World, excluding U.S.S.R. . .	93	94	100	103	110	96	84	69
(a) "Industrial" Europe . . .	91	87	103	106	112	103	90	(78) ⁴
(b) United States and Canada . .	95	98	97	101	109	87	74	58
(c) "Agricultural" Europe . . .	90	95	101	102	110	104	97	...
(d) Rest of the world (ten countries in Latin America, Africa, Asia and Oceania) . . .	91	98	99	103	109	112	103	...
B. World, including U.S.S.R. . . .	92	94	100	104	111	100	90	77
II. Indices of Production of Industrial Raw Materials :								
A. World, excluding U.S.S.R. . . .	93	94	99	103	111	100	89	76
B. World, including U.S.S.R. . . .	92	94	99	104	111	102	91	79

The movements of the sub-indices in this table are of considerable interest. The fall in production has been much smaller in agricultural Europe and in the group of chiefly agricultural countries in Latin America, Africa, Asia and Oceania than in the highly industrialised countries in Europe and North America.

Almost all the countries included in these two resistant groups have a comparatively young industrial system built up largely during and after the war.

The division made above between various groups of countries

¹ Institut für Konjunkturforschung.
² Economic Intelligence Service.
³ Provisional indices, subject to revision.
⁴ Rough estimate based on incomplete data.

may usefully be supplemented by reference to the following national indices of industrial production.

The index-numbers given in the table below show the course of industrial development for several countries in the four years 1929-1932 :

National Indices of Industrial Production in Certain Countries.
(Base : 1928 = 100.)

Country	Compiler of index	1929	1930	1931	1932
United States . . .	Federal Reserve Board . . .	107	86	73	58
Germany	Institut für Konjunkturforschung	100	90	74	61
United Kingdom	Board of Trade	106	98	89	88
France	Statistique générale	109	110	98	76
U.S.S.R.	Gosplan	124	156	189	205 ¹
Japan	Mitsubishi Econ. Research Bureau	111	106	101	108
Czechoslovakia	Dr. K. Maiwald	104	91	81	59
Belgium	Institut des Sciences économiques, Louvain	100	90	79	68
Sweden	Kommerskollegium	113	112	107	101 ²
Poland	Sveriges Industriförbund	106	102	89	84
Poland	Institut de Recherches sur le mouvement des affaires	100	82	69	54
Austria	Österreichisches Institut für Konjunkturforschung	103	87	76	66
Hungary	Inst. für Wirtschaftsforschung	98	85	69	61
Denmark	Statistiske Departement	108	118	108	...
Norway	Statistiske Centralbyrea	111	112	86	...
Canada	Dominion Bureau of Statistics	108	92	77	63

The production of manufactured commodities, except in the United Kingdom, where the home market has been sustained, has fallen more than that of raw materials, and the following table shows how great the disparity has been.

¹ Average January-September.

² Estimated on the basis of the Sveriges Industriförbundets Index.

The Production of Raw Materials and Manufactured Commodities.
(Base : 1929 = 100.)

Country	Production	1930	1931	1932
Canada	{ Mining	94	81	76
	{ Manufactures	83	72	63
U.K.	{ Mining	94	85	80
	{ Manufactures	91	84	84
U.S.A.	{ Mining	86	73	62
	{ Manufactures	80	67	53

The variant movements disclosed by the national indices of industrial production may be summarised roughly in the following comparison.

The Relative Decline in Industrial Production in Certain Countries, 1929-1932.

(World Average = 30.6.)¹

Countries in which the decline has been less than the world average	Countries in which the decline has been more than the world average
U.S.S.R. + 65	Belgium — 32
Japan — 3	Hungary — 38
Sweden — 11	Germany — 39
United Kingdom. — 21	Canada — 42
France — 30	Czechoslovakia . — 42
	Poland — 46
	United States . . — 46

Indices of industrial production are not available for many agricultural countries ; but there is much evidence that the decline in such countries was less than in most of the more highly industrialised States. The increased import restrictions which the agricultural countries imposed to protect their balances of payments and the strong movement towards industrial self-sufficiency are perhaps the strongest reasons for this development. The counterpart of increased agrarian production in the manufacturing countries has been an encouragement to industrial production in the agrarian countries. In both directions, the world has moved towards national self-sufficiency and away from international interdependence.

¹ Institut für Konjunkturforschung. U.S.S.R. included.

This conclusion is supported by the fact that export industries, despite the temporary stimulus given to them in many countries — the United Kingdom, Sweden and Japan, for example — by exchange depreciation, suffered more heavily than production for the home market. This fact may be inferred from the following table — the index-numbers both for production and trade referring to quantum, not values.

Indices of Industrial Production and Exports.
(Base : 1929 = 100.)

Country	Quantum of production			Quantum of manufactured exports		
	1930	1931	1932	1930	1931	1932
France	100	89	69	89	76	59
Germany	88	72	60	95	86	59
United Kingdom	92	84	83	82	63	63
United States	81	68	54	81	65	50 ¹

Three factors have been of special importance during 1932 in determining the volume of industrial production in different countries. The rapid strangulation of world trade has affected export industries directly, and domestic industries indirectly, by reducing world markets and depressing the prices of export commodities.

It is true that certain domestic industries have been temporarily stimulated by the exclusion of imports; but this partial and temporary stimulus to domestic industry, even in the most self-sufficient countries, has not gone far to compensate for the destructive effects of restricted international trade.

Exchange instability has also been a disturbing influence. In some of the countries which abandoned the gold standard, the export industries received an immediate, but in most cases a merely temporary, stimulus. This stimulus was limited by further falls in prices, increasing trade restrictions, and the generalisation of currency depreciation. On the whole, it was the home markets which were best sustained in the countries which abandoned the gold standard.

It would appear that those countries which maintained the gold standard in full operation during 1932 (*e.g.*, Belgium, France, the United States of America) and those which maintained the external value of their currencies by rigid exchange controls (*e.g.*, Germany, Austria and Hungary) or by import restrictions, which served much the same purpose (as in Poland), have found

¹ Estimate.

their industrial production decline most heavily, while those which departed from the gold standard (*e.g.*, the United Kingdom, Japan, Sweden) maintained their production at least for the domestic markets. On the other hand, recovery in the autumn of 1932 was most marked in the gold countries, and it is arguable that, by hastening and intensifying the liquidation of unsound businesses, these countries had taken the shortest cut to ending the depression.

Financial and monetary policies have also played a large part both in domestic and in export markets. Expansionist policies such as those described later in the chapter dealing with public finance appear, at least temporarily, to have maintained and even stimulated domestic production, while countries which were able, as was Japan, to control domestic costs, while the external value of their currency depreciated rapidly, were benefited in production for export.

While the circumstances of individual countries differ, however, there was a general diminution of production in 1932, with all its economic consequences of decreased purchasing power and employment, heavier overhead costs and financial instability.

THE POSITION OF THE INVESTMENT INDUSTRIES.

It is a characteristic of all depressions which follow an investment boom, that falling prices and reduced consumption as soon as the boom breaks reveal over-capacity and a sharp decline of production in the heavy industries producing capital equipment. The same phenomena are apparent in the present depression in an extreme degree; but the increased demand in the years of prosperity for goods manufactured for durable consumption, such as motor-cars and pianos, was followed by a drastic curtailment of their production when purchasing power was so greatly reduced in the depression. The investment boom was, in fact, largely based upon provision for a rapid increase in the consumption of such goods, and the drastic fall in standards of living, which has particularly affected non-essential and expensive consumption, has had the double effect of reducing the demand for, and therefore the production of, durable consumption goods and of thereby accentuating the decline in the production of investment goods, such as iron and steel products and machinery.

This phenomenon, new at least in its importance, may be described in another way by drawing a distinction between the older industries which cater for relatively simple and more essential consumers' demands and the newer industries which provide goods of durable consumption which are more expensive and less essential. The former have declined less and the latter

more during the depression. In the same way, it is the more durable types of producers' goods — locomotives and ships, for example — that have suffered most heavily as compared with the output of agricultural or textile machinery.

Running through this development also, as was noted in the *Survey* for 1931-32, there is a definite trend of industrial progress. Newer methods of production, newer industries and industries in the developing new countries have suffered on the whole less than the older types of production — electrical engineering less than steam, oil-driven ships less than steamers, motor transport (heavily hit as production has been in this line) less than railway materials, artificial silk less than other textiles. The following statistics, showing the output of various industries in Germany and the United States of America, illustrate the various factors at work.

The Decline in the Production of Various Classes of Commodities to the Lowest Point in 1932 as a Percentage of their Production in 1928-29. (Germany: 1928 = 100.)¹

Producers' goods	%	Consumers' goods	%
Wood-pulp	23	Paper	28
Machines	67	Textiles	29
Steel	68	Footwear	33
Rolling-mill products	71	Porcelain	62
Iron	73	Passenger cars	86
Lorries	88	Motor-cycles	90
		Pianos	95

(United States: 1929 = 100.)²

Producers' goods	%	Consumers' goods	%
Electrical goods ³	78	Foodstuffs	17
Cement (Portland)	79	Cigarettes	26
Trucks	81	Shoes	33
Locomotives, ⁴	86	Silk consumption	36
Electric motors ³	87	Books sold	37
Steel castings	90	Cotton textiles	48
Woodworking machines.	91	Gloves and mittens	62
Machine tools	92	Household furniture ⁵	76
Foundry equipment	95	Vacuum cleaners ³	79
		Domestic power pumps	89
		Passenger cars	91

¹ Calculated from the monthly returns published in the *Wochenbericht des Instituts für Konjunkturforschung.*

² Calculated from the monthly returns published in *The Survey of Current Business.*

³ Values: the quantitative reduction of output has been much less.

⁴ Decrease from the average of 1927-1929 to 1932.

⁵ Shipments expressed in working days' production, Grand Rapids District.

While there are obviously many special factors at work in different industries and while the general situation differs somewhat from country to country — as, for example, the greater saturation of the market reflected by the heavy decline in passenger-car production in the United States — the disproportion between the decline of production of producers' and consumers' goods is marked in every country and in the world as a whole.

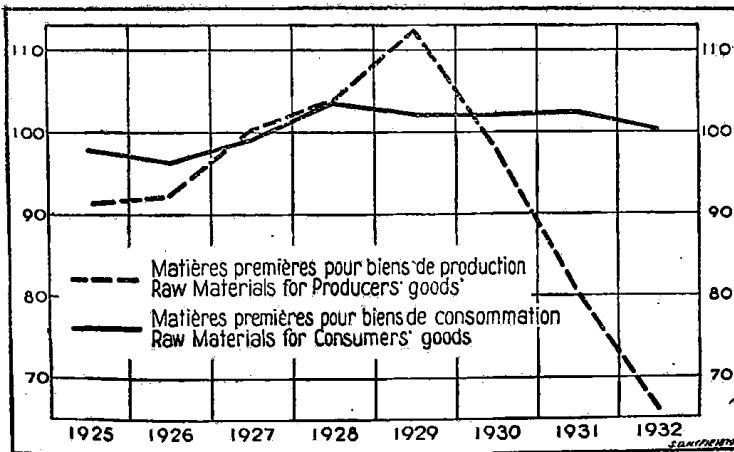
It can be illustrated first of all in the production of raw materials, which has been measured as follows :

World Production of Raw Materials, excluding U.S.S.R.
(Base : 1925-1929 = 100.)

	1925	1929	1930	1931 ¹	1932 ¹
Raw materials for producers' goods	91	112	98	81	66
Raw materials for consumers' goods	98	102	102	103	100

Indices of World Production of Raw Materials for Producers' and Consumers' Goods.

(Basis : Average 1925-1929 = 100.)



¹ Estimates.

Part of the explanation for these figures is clear when it is stated that, except for artificial silk, all the commodities which are reckoned as raw materials for consumers' goods are agricultural in origin. The index for this group is in fact governed by the production of cereals and meat, both of which have been well maintained. The production and consumption of foodstuffs has, as might be expected, diminished less than that of any other group of commodities during the depression.

The decline in the production of finished commodities of both categories is of course greater than the decline in the production of raw materials. The information that is available on this subject in national indices is reproduced in the diagram on page 91.

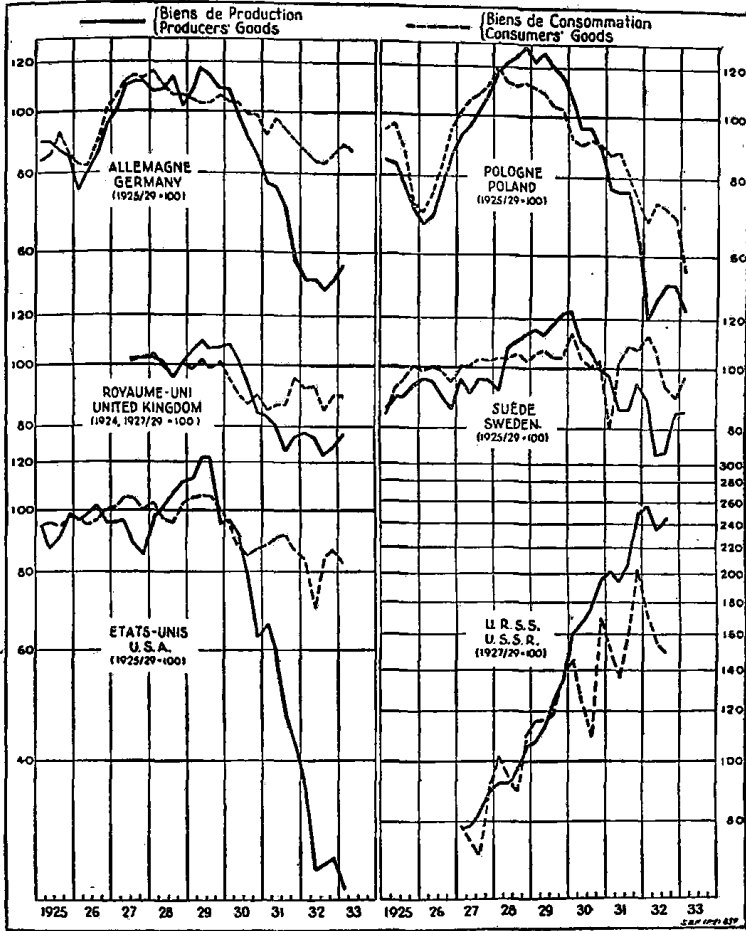
The figures are startling, especially the 1932 index of the production of producers' goods — iron and steel, tin and cement — in the United States, which fell to less than 30 per cent of the average production in the years 1925-1929, while at the lowest point in the third quarter of 1932 it was less than 20 per cent of the production in the corresponding quarter of 1929.

Nor did the quarterly figures for 1932 and the first quarter of 1933 give much ground for satisfaction, since the recovery in the fourth quarter of the year was slight and did not continue into 1933. The extent of the subsequent revival in May and June will be discussed in the last chapter of this *Survey*.

Quarterly Indices of Production of Producers' Goods, 1932-33.
(Base : Average 1925-1929 = 100.)

Country	1932				1933
	I	II	III	IV	I
Germany	54	55	52	54	58
United Kingdom (1924-1927-1929 = 100)	78	77	72	75	77
Poland	48	51	54	54	49
Sweden	89	73	73	85	85
U.S.S.R. (1927-1929 = 100)	257	234	244	...	...
U.S.A.	36	27	24	28	25

*Production Indices of Producers' and Consumers' Goods in Individual Countries. (Base : 1925-1929 = 100.)*¹



The German indices are further subdivided as follows :

	1925	1929	1930	1931	1932	
Producers' goods :	} Investment goods . . .	88	112	91	60	40
		} Other producers' goods	88	113	103	90	81
Consumers' goods :	} With elastic demand .		86	100	95	90	80
		} With inelastic demand	83	112	112	104	96

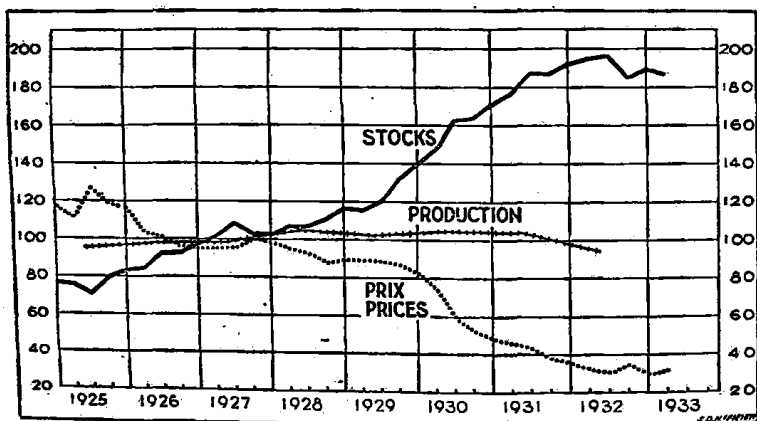
¹ Cf. League of Nations, *World Production and Prices, 1925-1932.*

THE ACCUMULATION OF STOCKS.

The accumulation of commodity stocks, which had been in evidence since 1925, appeared to reach its peak and begin to decline in the course of 1932. The information most readily available on this subject refers to visible stocks of raw materials, and in general only to those stocks retained by producers or in public warehouses. It is extremely difficult to obtain reliable indications of the stocks held at later stages of production — *e.g.*, by the manufacturers or by wholesalers.

While the statistics of stock accumulations contained in the table which follows are indicative of serious maladjustments between the demand and supply of the various products mentioned, they do not measure the extent to which overproduction or under-consumption exists at any particular moment. With this qualification, the statistics of stocks collected in various quarters may first be given in the form of total estimates for staple commodity stocks as a whole. Calculations have been made by the United States Department of Commerce and the German Institut für Konjunkturforschung in the attempt to arrive at such an index; and the results obtained by the United States Department of Commerce are reproduced in the following diagram :

General Index of World Stocks of Staple Commodities.



This general index may be supplemented by the statistics which show stocks of the most important raw materials and foodstuffs in more detail.

Indices of World Stocks of Primary Commodities.
(Base : 1925-1929 = 100.)

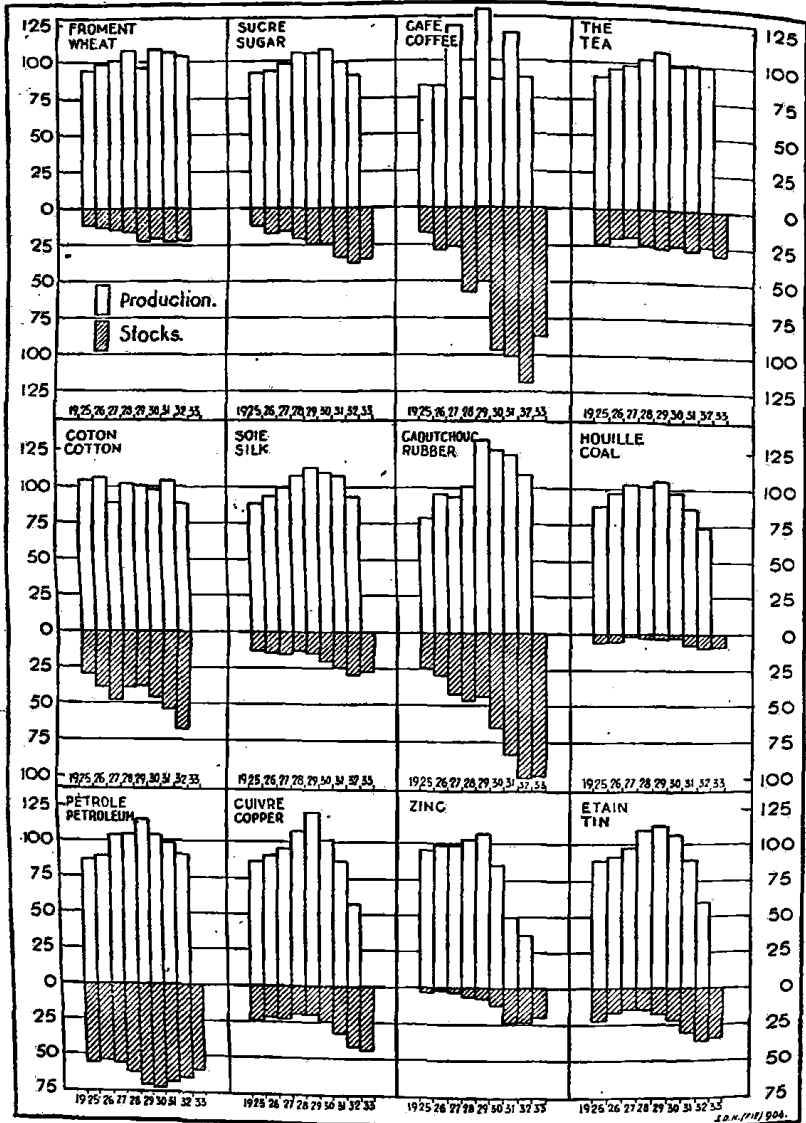
Date	General world index ¹	Wheat ^a	Sugar	Coffee	Cotton : world visible supply	Natural silk	Rubber	Petroleum (U.S.A.)	Copper	Lead (U. S. A. and U.K.)	Zinc (U. S. A. and U.K.)	Tin
1925 average	76	72	70	43	80	89	63	91	109	41	56	117
1926 "	89	76	103	73	98	90	80	90	108	73	56	89
1927 "	104	90	89	85	117	103	111	95	104	110	111	83
1928 "	108	112	109	150	101	102	118	105	85	117	134	92
1929 "	124	150	129	149	103	116	129	118	94	159	144	118
1930 "	158	155	157	243	127	174	183	118	153	311	356	169
1931 "	183	167	209	259	151	193	230	109	167	544	467	218
1932 "	194	163	230	284	161	193	262	105	(206)	730	448	219
1930 January . . .	140	181	157	204	141	153	159	118	125	198	245	136
April	148	161	171	246	128	137	177	120	146	.	297	155
July	163	118	173	256	104	163	178	119	159	.	359	184
October	164	169	101	267	117	210	200	115	164	.	435	179
1931 January . . .	172	181	196	262	173	205	210	113	161	423	464	191
April	177	187	236	253	163	168	227	111	155	.	464	218
July	189	138	196	230	132	160	226	110	171	.	477	225
October	186	156	190	277	124	212	236	105	189	.	458	225
1932 January . . .	192	189	240	300	178	238	267	107	204	664	458	224
April	196	185	254	300	168	200	268	107	.	.	458	224
July	196	138	226	256	143	172	255	105	.	.	464	222
October	184	155	196	.	144	191	258	103	.	.	422	213
1933 January . . .	189	184	244	249	184	216	269	99	213	795	415	207
April	187	.	249	219	171	178	267	99	...	.	454	190

Note. — The above indices should be interpreted in the light of the various explanatory notes which will be found at the foot of Table 6, Appendix I, of the League of Nations *World Production and Prices*, Geneva, 1933.

¹ General world index : based on the following nine commodities, the weights being indicated in parentheses : Cotton (9) ; sugar (6) ; wheat (6) ; rubber (3) ; coffee (2) ; copper (2) ; silk (2) ; tea (1) ; tin (1). The weights have been allocated in accordance with the value of the stocks on hand in the original base period, 1923-1925. All series, except those for copper and tin, are adjusted for seasonal variations (U.S. Dept. of Commerce ; *Survey of Current Business*, Annual Supplement, 1932, and subsequent numbers).

^a Wheat : calculated from Broomhall's visible supply.

Production and Stocks of Staple Commodities. 1



¹ Cf. Akerman : "Det Ekonomiske Läget", 1932, No. 1, page 15, Stockholm:

It will be observed that, while the stocks of certain commodities increased in 1932 — sugar 1.8 per cent, tea 10 per cent,¹ cotton 3.5 per cent, rubber 0.9 per cent, copper 4.6 per cent, lead 20.8 per cent,² other stocks decreased and the indices of world stocks as a whole were lower in the early months of 1933 than they had been a year earlier. The German index, for example, had fallen at the end of March 1933 by 5 per cent compared with the end of March 1932.³ It is a reasonable inference that, in 1932, for the first time since the depression began, current production did not exceed the industrial buying of raw materials. Many factors are responsible for this change, the most obvious being the drastic reduction of production in the case of many important commodities, particularly those of mineral origin. As credit became cheaper and confidence revived in the autumn of 1932, the manufacturing industries and the wholesale trade began to replenish their stocks which had run down considerably during the depression.

This fact renders more important a study of the size of the accumulated stocks relatively to current production and consumption. The world's total stocks of wheat on August 1st, 1932, represented about 20 per cent of that year's harvest; sugar stocks at the end of the harvest year 1932 were about one-third of the production in that year; copper stocks were rather more than three-fourths of the 1932 production; world stocks of coffee at the end of 1932 represented fifteen months' consumption at current rates; rubber stocks represented a year's consumption and stocks of American cotton on August 1st, 1932, nearly a year's cotton-mill consumption. These estimates, however, may quickly be rendered unreliable by a recovery in industrial production and therefore in the demand for raw materials, or merely by buying on the part of manufacturers with depleted stocks. Such buying is more likely to take place when prices appear to be rising again.

The statistics of stocks, either of raw materials or of finished products in the hands of manufacturers, are very scanty and unsatisfactory. In particular, it is difficult to get quantitative records, and the best material available consists of the value of stocks as disclosed by industrial censuses, tax statistics and similar sources. Inevitably these are considerably out of date before they are published and the table which follows therefore contains no information beyond 1931. In the case of Germany, it is known, however, that commodity stocks of the limited

¹ In the United Kingdom only.

² In the United States only.

³ *Wochenbericht des Instituts für Konjunkturforschung*, 6 : 8, May 24th, 1933.

*Stocks of Raw Materials and Finished Goods held by Manufacturers
at End of Year. ¹*

(National currency, 000,000's.)

Country	Kind of stocks	Currency	1923	1924	1925	1926	1927	1928	1929	1930	1931
Germany	Joint-stock companies — All stocks	RM.	7,500	9,700	11,100	10,100	11,600	13,000	12,600	11,000	9,000
	Craftwork — All stocks	RM.	1,100	1,400	1,600	1,500	1,700	1,800	1,800	1,500	1,100
Hungary	Joint-stock companies — Raw materials	Pengő	.	.	111	144	146	160	167	150	123
	Joint-stock companies — Finished goods	Pengő	.	.	221	263	305	348	352	332	288
	Census of Manufactures	Pengő ^b	146	240	279	293	369	391	412	428	341
Italy	Joint-stock companies — All stocks	Lira	6,881	8,166	10,272	10,625	10,377	9,190	9,750	9,429	(8,088)
Latvia	Joint-stock companies — All stocks	Lat	.	20	58	65	71	86	105	108	100
Netherlands	Joint-stock companies — All stocks	Florin	82	90	95	99	101	112	159	124	(92)
Norway	Census of Manufactures — All stocks	Krone	.	.	.	.	451	449	436	507	484
Poland	Joint-stock companies — All stocks	Zloty	.	.	.	549	719	972	1,163	....	...
Roumania	Joint-stock companies — Raw materials	Lei	878	1,376	1,515	1,982	1,772	3,947	3,271	1,956	2,063
	Joint-stock companies — Finished goods	Lei	5,217	7,744	8,921	8,907	9,376	9,004	10,399	11,356	8,034
United Kingdom.	Joint-stock companies — (Industrial and Mining) — All stocks	£	575	576	610	594	576	556	572	458	401

¹ Germany: Institut für Konjunkturforschung, *Sonderheft* 32, page 22. Estimate of total stocks based on official statistics.
Hungary: *Annuaire Statistique*, 1926-1931. (a) Stocks held by joint-stock companies; (b) stocks held by factories included in the census.

Italy: Societa Italiana per Azione, *Notizie Statistiche*. Stocks held by joint-stock companies.

Latvia: *Annuaire Statistique*. Stocks held by joint-stock companies.

Netherlands: *De Nederlandsche Conjunctuur*, March 1933, page 17. Stocks held by sixty-two companies.

Norway: *Norges Industri*. Stocks held by companies included in the census. Figures are yearly averages.

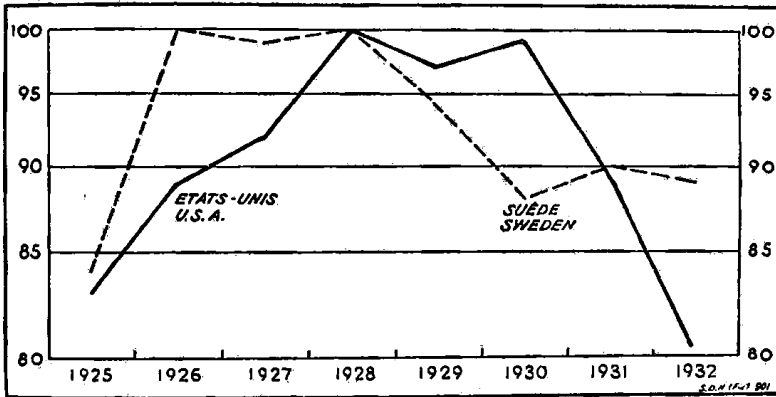
Poland: *Annuaire Statistique*, 1928-1930. *Information Statistique*, 1933. Fasc. spécial III. Stocks held by Polish joint-stock companies.

Roumania: *Annuaire Statistique*, 1930-1932. *Buletinul Statistical*, 1925-1932. Stocks of joint-stock companies.

United Kingdom: Colin Clark: "The National Income", Appendix I. Estimate of total stocks based on *Economist's* statistics.

liability companies which published their balance-sheets in the three first quarters of 1932 had a much lower value in 1932 (809,700,000 RM.) than the same companies' commodity stocks in 1931, when they amounted to 1,010,300,000 RM. It would seem, however, that, even in 1931, the value of manufacturers' stocks had begun to decrease. Some part of the decrease was obviously caused by the fall in prices; but it is almost impossible to say how great a part, because very little is known of the prices of the particular finished goods of which the manufacturers' stocks are composed, or of the weights which have to be attributed to each group of prices. Quantitative indices exist for Sweden and the United States and are shown in the following diagram. It would appear that, in Sweden, stocks at the end of 1932 were about 10 per cent, and, in the United States, 20 per cent less than in 1929.

Stocks of Finished Goods held by Manufacturers in the United States and Sweden, at End of Year.
(Base : 1928 = 100.)



Corroboration for these indications of diminished stocks in the hands of manufacturers may be obtained from the statistics of raw-cotton stocks, which are accurately known. The manufacturers' stocks of raw cotton at the end of January in successive years were:

	Bales (000's)
1929	5,294
1930	4,931
1931	4,586
1932	4,608
1933	4,542

Statistics of retail stocks can now be obtained from either complete or sample studies in three countries. The statistics shown below for Germany represent estimates for the total retail stocks of the whole country ; those for the United Kingdom and the United States are sample estimates for typical important areas.

*Retail Stocks in Germany, the United Kingdom
and the United States.¹*

	Germany		United Kingdom		United States	
	Total retail trade		Department stores, co-operative societies, shops under multiple or independent management		Department stores	
	Value RM. (000,000,000's)	Quantum change from previous year ² %	Value at cost : March 1930 = 100	Quantum change from previous year ² %	Value at cost : yearly average, 1923-25 = 100	Quantum change from previous year ²
End of year						
1929 . . .	8.1	— 2	—	—	94	—
1930 . . .	7.2	— 12	—	—	85	+ 3
1931 . . .	5.7	— 21	—	—	73	+ 1
1932 . . .			—	—	56	— 10
March						
1930 . . .			100	—	100	—
1931 . . .			88	— 6	87	+ 2
1932 . . .			86	—	72	—
1933 . . .			80	— 2	55	— 12

There is some evidence, therefore, that stocks in the hands both of manufacturers and of retailers are considerably depleted. This lends more importance to the reduction of visible stocks of raw materials during 1932.

¹ Germany: Institut für Konjunkturforschung, *Sonderheft 32*.

United Kingdom: Bank of England, *Statistical Summary*, April 1933.

United States: *Survey of Current Business*.

² Calculated by the Institut für Konjunkturforschung.

³ Calculated on the assumption that prices varied as the cost-of-living index.

⁴ Calculated on the assumption that prices varied as the mean of the National Industrial Conference Board's retail price indexes of food and clothing.

Chapter IV.

WAGES AND SOCIAL POLICY.

THE SHRINKAGE OF WAGES.

The *Survey* for 1931-32 drew attention to certain aspects of the distributive conflict which underlies much of the controversy concerning the nature of and remedies for the depression.¹ It was pointed out that standards of living had risen appreciably in the post-war period and that there was much greater resistance than previously to any attempt at lowering them. Wage-rates were higher, conditions of labour had improved, hours had been shortened and a much larger part of real income was provided by public services, while in most countries there had been a great extension of social insurance. By the spring of 1932, however, it was becoming evident that national incomes had fallen so heavily that the continuance, not only of existing wage-rates and labour conditions, but also of governmental expenditure upon social purposes was seriously challenged. In the year that has since elapsed, national incomes have fallen to still lower levels and the dilemma described in the *Survey* for 1931-32 has therefore become more acute. The present chapter is devoted to a further consideration of the distributive conflict involved in labour and social policy at the present time.

The facts of declining production and falling prices set out in the preceding chapters leave no room for doubt as to the great extent of the fall in national incomes since 1929. Exact measurement is, of course, not possible, and up-to-date estimates are available for only a few countries ; but no country has gone unscathed, and, in most, the decline both of real and, still more of nominal, income has been very great. No criteria exist, beyond the production estimates already discussed, by which real income may be measured ; but the estimates of the value

¹ Chapter VIII.

of national incomes quoted below show for most countries a greater fall during the depression than the fall in average price-levels. There has been, in addition to changes in the value of the monetary units and to the violent redistributions of income occasioned thereby, a very substantial fall in the real amount of goods and services available for distribution.

The Fall in National Incomes.

(000,000's omitted.)

60-70,000

Country	Unit	1928	1929	1930	1931	1932
Australia ¹	£A.	645	556	459	(430)	...
Germany ²	RM.	75,400	76,100	70,200	57,100	(46,700)
Italy ³	Lira	94,400	—	—	(6,000-7,000)	...
New Zealand ⁴	£NZ.	150	142	117	100	...
Norway ⁵	Krone	2,153	2,200	2,197	1,994	...
Roumania ⁶	Lei	191,400	184,900	138,900	105,600	(90,000)
United Kingdom ⁷	£	3,849	3,996	3,938	3,499	3,199
United States ⁸	\$	82,400	85,200	70,700	(52,700)	(40,000)
U.S.S.R. ⁹	Pre-war Roubles	18,600	—	22,600	31,200	...

The magnitude of the fall in national incomes is all the more impressive, since it interrupts a long trend of increase. For decades before the war there was in almost every country a strong upward tendency, interrupted but slightly during the long period of rising prices, when both the duration and the violence of cyclical depressions was minimised. This progress was resumed by increasing production as well as rising values after the first post-war crisis checked the great expansion of the war period. The world, therefore, was habituated to steadily increasing national incomes and rising standards of living.

¹ Committee appointed by the Government of the Commonwealth of Australia, "Preliminary Survey of the Economic Problem", Report April 1932 (the figures refer to the years 1928-29 to 1931-32).

² Statistisches Reichsamt, "Das deutsche Volkskeinkommen", Berlin, 1932. Institut für Konjunkturforschung, *Vierteljahrsheft*, February 1933.

³ Institut International de Statistique. *Bull.* XXV, Livraison 3. Professor Gini's estimate, page 365. "The Association of Italian Corporations Business and Financial Report", June 1st, 1932.

⁴ Canterbury Chamber of Commerce, *Bulletin*, April 1933 (figures refer to years 1928-29 to 1931-32).

⁵ "Statistiske Meddelelser".

⁶ *Buletin Trimestrial al Institut Romanesc de Conjunctura*, 1933, No. 1-2.

⁷ CLARK: "The National Income", London, 1932. *The Economic Journal*, June 1933.

⁸ *National Industrial Conference Board Bulletin*, February 20th, 1933.

⁹ *Sowjetwirtschaft und Aussenhandel*, No. 5, 1932.

The proportion of national incomes paid to wage-earners was of less importance than the increase in the total amount available for distribution. Since the depression, the share of national incomes going to the wage-earning and salaried classes appears to have been increasing in many countries; but the total has been so greatly reduced that the absolute amounts paid to wage-earners have fallen very heavily. Thus, in the United States, wages and salaries, which in 1929 had absorbed 62.5 per cent of the national income, by 1932 absorbed 70.5 per cent; but the actual amounts paid had fallen from \$53,300 million to \$28,200 million.¹ The table printed below shows the proportion of national incomes devoted to the payment of wages and salaries.

*The Percentage of National Income Paid as Wages and Salaries.*²

Year	Belgium		France (post-war territory)	Germany (post-war territory)	United Kingdom *		United States (Continent)	
	Wages	Wages and salaries	Wages and salaries	Wages and salaries	Wages	Wages and salaries	Wages	Wages and salaries
1913 . .	34.0	—	43.6	45.3	42.7 ⁴	54.5 ⁴	36.4	51.8
1924 . .	38.0	—	46.4	—	41.5	63.3	37.7	56.1
1925 . .	—	—	44.6	56.3	—	—	37.6	55.9
1926 . .	—	—	43.6	55.5	39.2	63.0	*38.1	56.8
1927 . .	41.5	55.3	44.1	54.9	40.8	63.5	*37.3	56.8
1928 . .	—	—	44.4	56.5	40.9	64.2	*36.0	56.0
1929 . .	—	—	—	56.6	39.8	62.4	...	—
1930 . .	40.6	52.6	—	*56.4	38.9	61.4	...	...
1931 . .	—	—	—	*57.9	41.4	65.7	...	...
1932 . .	...	...	...	...	...	*72.1	...	...

¹ *National Industrial Conference Board Bulletin*, February 20th, 1933; *Bradstreet's Weekly*, November 12th, 1932. These figures are based on the National Industrial Conference Board's estimate of national income and should not be compared with the figures given in the table above, which are based on King's estimates.

² Sources:

Belgium, F. BAUDHUIN: quoted in *Bulletin de Statistique et de Législation comparée*, November 1927, pages 767-768; and F. BAUDHUIN: "Le revenu national en 1930", in *Bulletin d'Information et de Documentation de la Banque nationale de Belgique*, 5th year, Vol. I, pages 373-377.

France, M. HUBER: "La population de la France pendant la guerre, avec un appendice sur les revenus avant et après la guerre", pages 942 and 957.

Germany, "Statistisches Jahrbuch für das Deutsche Reich", 1932, page 526.

United Kingdom, C. CLARK: "The National Income, 1924-1931", pages 72 and 140. 1932, *The Economic Journal*, June 1933.

United States, W. I. KING: "The National Income and its Purchasing Power", page 80.

³ Based on home income only.

⁴ Figure for 1911.

* Provisional.

The situation varies a good deal from country to country, and in the absence of more complete and up-to-date statistics it is not possible to state a definite trend. The position is clearest in the United Kingdom, where wage-rates have been strongly maintained. Statistics of industrial production for a number of smaller countries suggest that the tendency has been very strong for the total wages paid to become a smaller percentage of the national income. In the majority of cases, the percentage which wage and salary payments represent of the net value of industrial production has fallen substantially. This appears to indicate that overhead capital costs have been more difficult to reduce than wages.

*Percentage of Wages (W) and Wages and Salaries (WS) to the Net Value of Industrial Production.*¹

Year	Australia		Canada		New Zealand	Finland	Hungary		Latvia	Norway	
	(WS)	(W)	(WS)	(W)	(WS)	(W)	(WS)	(W)	(W)	(WS)	(W)
1926 (1926-27)	55.8	43.8	33.6	52.0	.	36.8	32.5	24.6	.	.	.
1927 (1927-28)	54.6	42.4	32.5	52.1	.	35.5	35.2	28.1	.	49.3	38.5
1928 (1928-29)	54.3	41.5	31.9	51.3	.	36.2	35.8	28.4	38.8	48.0	38.1
1929 (1929-30)	54.2	40.7	31.3	51.4	50.4	36.7	36.0	28.4	40.8	47.5	38.2
1930 (1930-31)	52.8	41.8	31.3	52.0	50.8	36.2	35.3	26.8	41.9	49.0	39.1
1931 (1931-32)	50.4	42.4	29.7	.	49.7	33.2	36.4	27.9	44.5	49.2	37.1
1932 (1932-33)											

While the fall in aggregate wage payments illustrated below is a most impressive and important fact, the maintenance of nominal wage-rates at relatively high levels demonstrates the

¹ The figures are for calendar years, except for Australia (years ended June) and New Zealand (years ended March). Salaries do not include working proprietors' income, except for New Zealand. Net output is computed by deducting from the gross value of output the cost of materials and fuel and electricity used. In the case of Canada and New Zealand, only the cost of material used, but not of fuel, has been deducted; and, in the case of Finland, the cost of electricity used has not been deducted. The figures refer, in general, to manufacturing industries, but include mining, quarrying, building and construction of works, and gas, etc. The first column for New Zealand includes tramways, the second not.

Sources:

Australia: "Official Year-Book, 1931-32"; "Quarterly Summary of Australian Statistics", March 1933. — Canada: "Official Year-Book, 1932"; "Advance Report on the Manufacturing Industries 1931". — New Zealand: "Official Year-Book, 1933"; "Monthly Abstracts of Statistics", January 1933. — Finland: "Teallisuustilasto, Industristatistik 1931", Helsingfors, 1933. — Hungary: "Annuaire Statistique 1926-30", "Revue Hongroise de Statistique", Septembre 1932, "Supplément", Octobre 1932. — Latvia: "Annuaire Statistique 1931". — Norway: "Norges Industrie 1931", Oslo, 1933.

importance attached by the wage-earners to the maintenance of hardly won nominal standards. It is significant that, despite the overwhelming nature of the depression and its costs, money rates of wages in most countries have not fallen as fast as the cost of living. In the table and diagram which follow, quarterly indices of nominal wage-rates, or in certain cases, of hourly earnings are given for the three depression years 1930-1932.

It is clear that, except in the case of agricultural wages in the United States, the indices may be divided into two groups, the first of countries (Czechoslovakia, Denmark, France, the United Kingdom) where nominal wage-rates have been sustained around the 1929 levels, and the second of those, including both agricultural and industrial countries, where rates have been cut from 15 to 20 per cent. The annual figures for many other countries, giving separate indices for different major occupations, indicate that the number of instances in which wage-rates have been maintained or have fallen slowly is considerably greater than those where deflation policies have forced drastic reductions.¹ It is not difficult to pick out particular industries in different countries in which the rates have been reduced much more than the average; but when the violence and persistence of the depression is considered, it is remarkable to find how generally the rates have been maintained.

Even where cuts have been general, they have not usually been as great as the recorded fall in the cost of living. It is true that the index-numbers which measure average movements of the retail prices of food, clothing, heat and light, rent, and in some cases even miscellaneous expenses, may not exactly fit the circumstances of particular groups or even the majority of wage-earners in a period of rapid change. But index-numbers of real wages, compiled by correcting the nominal wage-rates given above for changes in the cost of living, show such a general tendency to rise that there can be little doubt that most wage-earners in constant full-time employment at standard rates are, except for the loss of supplementary earnings such as overtime, in a much better position than in 1929.

¹ Cf. most recent tables in *International Labour Review*.

Index-Numbers of Nominal Wages in Various Countries.
(Base : 1929 = 100.)

Country	1930				1931				1932				1933	
	III	VI	IX	XII	III	VI	IX	XII	III	VI	IX	XII	III	VI
Australia ¹	100	99	97	95	92	90	88	87	86	86	82	81	...	...
Czechoslovakia ²	101	103	103	103	103	103	103	103	103	103	103	103	102	...
Denmark ³	100	102	102	104	102	102	102	103	102	102	102	103	...	...
France ⁴	107	108	108	108	108	103	103	99	94	95	95	...	...	...
Germany ⁵	102	102	102	101	97	96	95	84	84	81	80	80	80	...
Italy ⁶	99	101	99	94	90	92	89	88	85	87	86	85	*85	...
Japan ⁷	100	98	96	95	94	92	92	91	90	89	89	88	*82	...
New Zealand ⁸	100	100	100	100	100	89	89	89	87	86	84	83	83	...
Poland ⁹	101	101	100	98	95	94	93	91	88	87	84	83	*81	...
United Kingdom ¹⁰	99	99	99	99	99	98	97	97	96	96	96	96	95	...
U.S.A. (Industry) ¹¹	100	100	100	98	98	96	95	91	88	85	81	79	78	...
U.S.A. (Agriculture) ¹²	94	92	88	77	74	71	66	58	56	51	49	44	43	...

¹ Men : hourly rates. Mines, industries, public service, commerce, etc. ; for end of month (Commonwealth Bureau of Statistics).

² Men and women : hourly minimum rates. Industries, average of month (Statistical Office of the Czechoslovak Republic).

³ Men and women : hourly earnings. Industries, public service, commerce, etc. ; average for the quarter ending with the given month (Department of Statistics).

⁴ Men : daily earnings. Mines ; average for the quarter ending with the given month (Statistique générale de la France).

⁵ Men and women : hourly rates. Mines, industries, public services ; first of following month (Statistisches Reichsamts).

⁶ Men and women : hourly earnings. Mines, industries, public services, etc. ; average of the month (Central Institute of Statistics).

⁷ Men and women : daily rates. Industries ; end of the month (Bank of Japan).

⁸ Men : weekly minimum rates. Agriculture, mines, industries, public services, commerce, etc. ; average for the quarter ending with the given month (Census and Statistics Office).

⁹ Men and women : daily rates. Mines, industries ; end of the month (Central Office of Statistics).

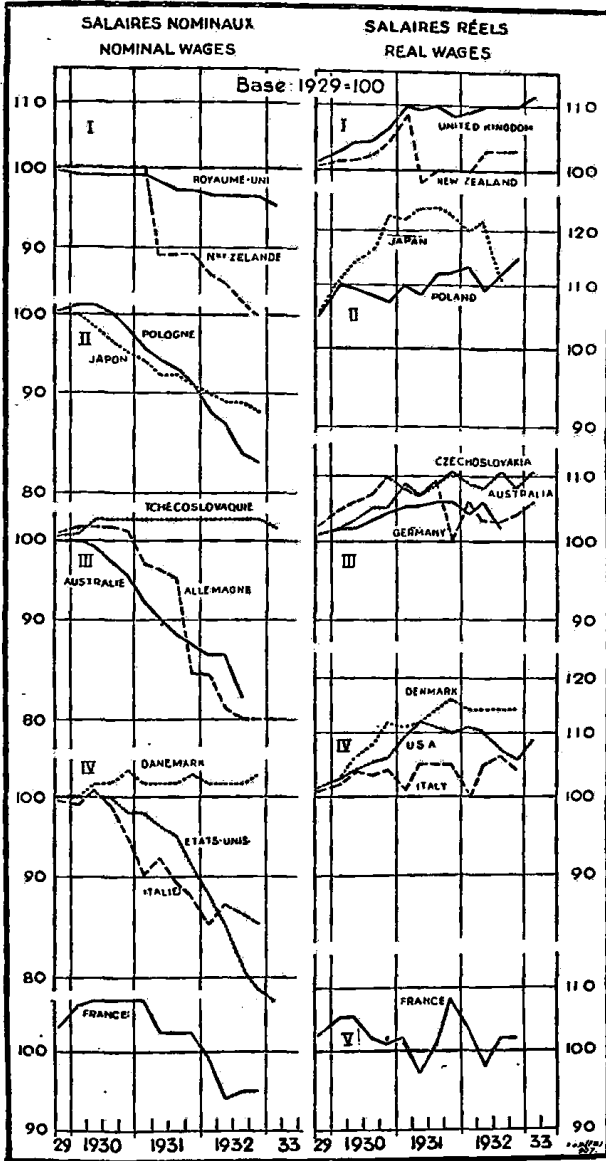
¹⁰ Men and women : weekly rates. Agriculture, mines, industries, public services ; average for the quarter ending with the given month (Ministry of Labour).

¹¹ Men and women : hourly earnings. Various industries ; first week of the given month (National Industrial Conference Board).

¹² Men : daily rates. Agriculture ; first of the following month (United States Department of Agriculture).

* February 1933.

Index-Numbers of Nominal and Real Wages 1930-1933.
(Base : 1929 = 100.)



I: Weekly rates. II: Daily rates. III: Hourly rates. IV: Hourly earnings. V: Daily earnings.

*Index-Numbers of Real Wages in Various Countries.*¹
(Base : 1929 = 100.)

Country	1930				1931				1932				1933
	III	VI	IX	XII	III	VI	IX	XII	III	VI	IX	XII	III
Australia . . .	102	102	103	104	105	105	106	106	104	106	102	102	...
Czechoslovakia .	102	103	105	105	109	107	109	111	109	108	111	108	111
Denmark . . .	103	106	108	112	111	112	114	116	114	114	114	114	...
France . . .	105	105	102	101	102	97	101	108	103	98	102	102	...
Germany . . .	105	106	107	110	108	107	109	100	106	103	103	104	106
Italy . . .	102	104	103	104	101	105	105	105	100	105	106	104	*101
Japan . . .	111	114	116	123	122	124	124	123	120	122	117	111	*109
New Zealand . .	101	101	102	104	108	98	100	100	100	103	103	103	104
Poland . . .	110	109	108	107	110	108	112	112	113	109	112	115	*113
United Kingdom	103	104	104	106	110	109	110	108	109	110	110	110	112
United States :													
Industry . . .	103	104	105	106	110	112	111	110	111	110	107	106	109
Agriculture . .	96	95	92	83	83	83	77	70	70	65	64	59	61

The fortunate position of those workers who remain in steady employment, while important from the point of view of maintaining standards of remuneration which may become general again when the depression passes, is overshadowed by the heavy fall of earnings. There has been a widespread reduction of overtime and a considerable spreading of work by various methods of short-time or irregular employment in addition to a great increase in total unemployment. Unemployment demands special attention in a separate section ; but examples may be given here of the losses occasioned to the wage-earners by diminished overtime earnings and the greater irregularity of employment.

The report published by the International Labour Office as a preliminary to the Preparatory Conference on Hours of Work and Unemployment held at Geneva in January 1933 summarises the statistical information available concerning both these problems.² Practical difficulties limit the possibilities of eliminating overtime. A sudden emergency, while not adequate to warrant the engagement of fresh workers, may demand extra hours from the existing staff. The average amount of overtime per worker employed on overtime has somewhat decreased ; but the number of workers so employed has been much more reduced. Thus, in Czechoslovakia in 1929, over 287,000 employees worked an average of 57 overtime hours in the year, while in 1931 only 90,000 worked an average of 47

¹The index-numbers of nominal wage-rates used in the preceding table corrected by the official indices of the cost of living.

²International Labour Office, "Hours of Work and Unemployment", Geneva, 1933.

* February 1933.

overtime hours. In the Netherlands, the number of industries receiving overtime permits increased continuously from 1923 to 1929, but fell considerably in 1930 and 1931. In Belgium in 1929, over 49,000 workers had a total of over 4 million overtime hours, but in the twelve months ending September 30th, 1932, these figures fell to less than 6,000 workers with 391,000 hours of overtime.¹

There was also a very considerable extension of short time and irregular work, reflected in the statistics of the partially or intermittently unemployed in many countries.² Special enquiries made by the International Labour Office at various dates in 1932 showed large percentages of workers affected by short time in almost every country, and in some industries in all countries, for which statistics were available. Thus the American Federation of Labour estimates that, in addition to an unemployment percentage of 32 in September 1932, a further 32 per cent of those employed were working short time. The short-time percentage was as high as 50 in some trades. In Italy in August 1932, the percentage of workers employed for less than a full working week was almost 30 for all industries and was as high as 61.8 in hatmaking. In the United Kingdom in September 1932, short time affected percentages of the workers employed ranging from 13 in carpet-making to 46 in the boot and shoe industry. In Germany during 1931, similar high percentages were recorded for many industries, and in June 1932 a sample enquiry revealed 33.7 per cent of the salaried workers employed as on short time also.³ The position in France is clear from the following table :

*Hours of Work in French Factories and Mines.*⁴

Date	Distribution of occupied workers (per thousand) according to the number of hours worked weekly			
	Forty-eight hours or more	More than forty and less than forty-eight hours	Forty hours	Less than forty hours
1930 : June . . .	969	24	5	2
December	936	45	11	8
1931 : June . . .	697	175	69	59
December	545	217	91	147
1932 : June . . .	489	178	105	228
December	615	188	84	113

¹ International Labour Office, "Hours of Work and Unemployment", pages 34-37 and 187, Geneva, 1933.

² For the most recent estimates of intermittent unemployment, see current issues of the League of Nations *Monthly Bulletin of Statistics*.

³ "Hours of Work and Unemployment", *op. cit.*, pages 26-32 and 177-186.

⁴ Which are subject to factory inspection and occupy more than 100 persons. *Bulletin de la Statistique générale de la France*, January-March 1933.

Historical data are not available to determine the extent to which short-time practices have grown in other countries during the depression, but the statistics showing the rapid growth of partial unemployment undoubtedly reflect the influence of such an increase. The table below gives such statistics as bearing upon, if not exactly measuring, this problem.

*Partial or Intermittent Unemployment Percentages in Various Countries, 1929-1932.*¹

Country	1929	1930	1931	1932
Germany	7.5	13.4	20.0	22.6
Belgium	3.0	7.9	16.9	20.7
United Kingdom	2.2	4.3	4.6	4.5
Switzerland	1.7	7.2	12.1	12.2

In view of these statistics and of the facts relating to unemployment discussed in the next section, it is not surprising to find that the aggregate earnings of the wage-earners have decreased very greatly in most of the countries for which statistics are available.

In Germany, for example, between 1929 and 1932, pay-rolls dropped from RM. 44,500 million to RM. 25,700 million.² In the United States in the same period the drop was even greater, amounting to 60 per cent. In Italy, the totals fell from 6,040 million lire in 1929 to 4,100 million in 1932. Real wages obviously fell rather less; but it is estimated that, even allowing for the fall in the cost of living, "the purchasing power of the wage-earning population shrank by 48 per cent in the United States, by 20 per cent in Germany, and by 19 per cent in Italy between 1929 and 1932".³ In the United Kingdom, the fall in money-wages was much less than the figures cited above. It is estimated that in that country "the shrinkage in money-wages amounted to 7 per cent between 1929 and 1931 and probably to about 10 per cent between 1929 and 1932"³. The cost of living at the end of 1932 was about 13 per cent lower than the monthly average in 1929, so that the aggregate of real wages would appear to have increased in the United Kingdom.

¹ League of Nations *Monthly Bulletin of Statistics*.

² "Wochenbericht des Instituts für Konjunkturforschung", March 8th, 1933.

³ Report of the Director of the International Labour Office, June 1933.

The Relief of Unemployment.

During the year 1932, with few and partial exceptions, the volume of unemployment continued to increase throughout the world. The Director of the International Labour Office, in the spring of 1932, estimated the number of unemployed as 20 to 25 millions. His successor's estimate of the number a year later, in early 1933, was 30 millions. The general tendency to increase is illustrated by the following table :

National Unemployment Statistics at the End of March 1929-1933.¹
(000's)

Country	1929	1930	1931	1932	1933
Australia	39	63	114	120	109
Austria	225	239	304	417	456
Belgium ²	28	42	207	350	383
Canada	12	23	32	77	80
Czechoslovakia	50	88	340	634	878
Danzig	18	20	27	36	38
Denmark	66	49	70	145	166
Estonia	4	4	3	8	15
Finland	3	10	11	18	19
France	9	14	72	347	356
Germany	2,484	3,041	4,744	6,034	5,599
Hungary	14	43	55	71	69
Irish Free State ⁴	19	23	25	31	83
Italy ²	309	413	735	1,085	1,111
Japan	—	352	397	474	—
Latvia	9	6	9	23	13
Netherlands	—	—	—	253	342
New Zealand	3	3	38	45	51
Norway	24	23	29	38	42
Poland	177	289	373	360	280
Roumania	10	13	48	55	—
Saar	9	9	18	45	42
Sweden	44	42	73	99	121
Switzerland ²	9	21	61	103	113
United Kingdom ²	1,204	1,694	2,666	2,660	2,821
United States ²	—	2,964	6,403	10,477	13,359
Yugoslavia	12	10	12	23	23

These statistics, compiled by different methods, represent somewhat different facts in the various countries and are comparable only as showing the trend in each country and not inter-

¹ League of Nations *Monthly Bulletin of Statistics*.
² Partial and intermittent unemployment included.
³ Figures for United States, 1930-1932; American Federation of Labour, see *Weltwirtschaftliches Archiv*, April 1933.
⁴ New series from June 1932.

nationally. The general trend of increase is sufficiently obvious to need little comment. In only eight countries — Australia, Canada, Germany, Hungary, Latvia, Poland, Saar and Yugoslavia — was there some decrease in the number of unemployed in March 1933 as compared with March 1932.

In passing, attention may be drawn to one significant effect of unemployment, the repatriation of imported labourers, which, while of very great importance for the countries immediately concerned, is apt to escape notice in general surveys of the situation. This phenomenon is of importance, not only in Europe, but also in such regions as Malaya, where immigrants provide a great deal of the transient labour used on plantations. The extent to which repatriation has proceeded may be illustrated by the following table showing the migration of foreign workers into and out of France.

Migration of Foreign Workers into and out of France.¹

	1929	1930	1931	1932
Number entered . . .	179,329	187,407	102,267	53,208
Number left	38,870	54,975	92,916	108,513

The major causes of this vast breakdown of organised employment are obviously those which have contributed to the economic and financial depression in general. In addition to the well-recognised monetary, financial and trading factors which have been repeatedly set forth in expert analyses of the circumstances, there are far-reaching structural changes proceeding in industry and trade.² These structural changes are geographical, affecting the localisation of important industries; technical, involving the transformation of productive methods; and social, arising from changing habits of consumption. It is clear that the world is in the midst of a period of rapid industrial change which, in addition to more temporary causes of monetary, financial and commercial paralysis, is gravely affecting the welfare of large masses of workers. The more temporary causes, with their mixed political, economic and financial background, are more appropriately discussed in later chapters of this *Survey*, and

¹ *Bulletin de la Statistique générale.*

² Cf. "Report of the Gold Delegation of the Financial Committee", Geneva, 1932; "Draft Annotated Agenda for the Monetary and Economic Conference", Geneva, January 1933; also "World Production and Prices, 1925-1932", Geneva, August 1933.

some of the outstanding structural changes were dealt with in the preceding volume.¹

Nearly all discussions of unemployment in recent months, however, have directed attention to various aspects of the effects of technical progress upon the demand for labour, particularly in the heavy industries. The statistics of unemployment by industries reveal the pressure that has been exerted by the depression upon the export industries of every country and particularly upon those in which technical progress is proceeding most rapidly. It is impossible to separate the influence of commercial restrictions and similar factors from the effects of technical and geographical changes in industrial structure, and it so happens that, in many important cases, both sets of influences are concentrated upon much the same industries. The summary table on the next page is reproduced from national statistics, which are not compiled upon strictly comparable bases; but there is sufficient evidence therein of a concentration of unemployment, except in the building trades, upon export rather than domestic, and upon the production rather than the consumption, industries.

The particular circumstances of certain industries need to be considered in each country and, in particular, some industries which in one country are largely dependent upon the export market, in other countries are almost wholly domestic.

The recent preoccupation with "the hard core of unemployment" caused by far-reaching structural changes of industry and commerce as distinct from the cyclical aggravation resulting from the crisis, while new to the present generation, has definite historical parallels in other periods of accelerated economic change, such as those which followed the rapid introduction of machinery after the Napoleonic wars and the advance of the chemical industries in the seventies. Such parallels, while throwing light upon the problem, do not alleviate its hardships to the workers. In the circumstances of free mobility and competition assumed by classical economic theory, it is easy to demonstrate that more efficient production in itself creates fresh demands for labour and so absorbs the unemployment it creates. The fresh demands for labour created by the manufacture of synthetic nitrates in Europe is, however, of little immediate help to the labourers thrown out of employment in Chile, and, when the pace of industrial change is as rapid and sustained as it has been in recent years, there arise real and intractable problems of persistent unemployment that are hard to solve

¹ "World Economic Survey 1931-32", Chapter I. See also report of the Director of the International Labour Office, June 1933.

even within national boundaries and still harder internationally. "Labour", in Adam Smith's phrase, "is of all commodities the most difficult to be transported".

*Statistics of Unemployment by Groups of Industry.*¹
(Percentage of Unemployed Workers at the End of March
in Successive Years.)

Country	Year	Build- ing	Engin- eering, etc.	Mining	Textiles	Print- ing	Food
Australia	1930	17.5	16.7	8.7	.	3.8	9.3
	1931	30.4	27.7	32.4	.	12.6	17.4
	1932	37.9	31.1	33.5	.	15.4	17.1
	1933	...	...	...	...	...	...
Belgium	1930	2.6	1.2	0.1	1.7	1.1	0.8
	1931	25.1	10.6	0.5	7.7	4.0	4.1
	1932	30.7	18.6	4.0	20.5	11.2	7.6
	1933	27.9	21.6 ³	4.5	17.6	12.8	9.7
Canada	1930	30.5	16.3	11.8	2.2	3.7	.
	1931	45.7	16.1	12.4	4.4	6.8	.
	1932	62.3	...	9.9	15.8	12.1	.
	1933	71.0	70.1	17.5	19.8	15.9	.
Germany ²	1930	53.1	15.9	4.5	12.9	13.3	14.1
	1931	73.9	29.3	13.4	21.6	22.2	24.1
	1932	88.7	43.6	18.8	30.7	35.0	31.9
	1933	87.5	50.0 ³	19.1	31.1	37.3	27.9
Netherlands	1930	13.7	6.2	0.4	9.2	2.8	5.3
	1931	29.9	23.7	0.4	21.7	4.5	12.6
	1932	41.6	40.6	36.6	27.3	10.9	17.5
	1933	...	...	...	...	...	...
Sweden	1930	27.7	7.6	13.9	3.7	4.9	10.4
	1931	40.8	17.0	21.5	3.8	5.0	11.7
	1932	47.6	26.0	39.6	5.1	8.9	14.8
	1933	55.3	27.3	37.4	9.7	11.5	17.9
United Kingdom	1930	16.0	13.7	14.3	25.5	6.0	10.3
	1931	22.5	26.6	27.4	36.5	10.1	13.2
	1932	29.0	27.2	26.9	23.4	11.2	12.5
	1933	27.2	28.6	31.2	26.0	11.1	13.4

There arises the dilemma, therefore, apart altogether from the solution of the present financial crisis, of mitigating the social effects of structural industrial change without placing undue obstacles in the way of the more efficient and economical production which such change may be expected to bring. As

¹ League of Nations *Statistical Year-Book*.

² Wholly unemployed only.

³ Metals.

⁴ Carpenters.

was pointed out in the last *Survey*,¹ industrial progress wins its way even during depressions, and, if higher standards of living are to be won by increased technical efficiency, industrial specialisation and rationalisation must be allowed to re-arrange both the localisation and the technical processes of manufacture. Merely obstructive measures of protection designed to protect existing arrangements of industry are both costly and in the long run probably futile. The more difficult, but ultimately more effective, line of attack upon the problem lies in constructive methods of promoting industrial mobility, fundamentally by revising educational methods so as to produce a more generalised, adaptable type of skill to meet the new conditions of labour.

In the meantime, however, there are heavy costs to be met. Public opinion no longer tolerates the harsh injustices which such periods of change in the past worked upon the unfortunate labourers whose skill suddenly became unmarketable. In every country, even in the strongholds of individualism, the necessity of relief and the advisability of such preventive measures as unemployment insurance, special training and assistance in gaining re-employment are recognised. The cost of such measures in recent years has become very great.

Schemes of unemployment insurance have proved inadequate to carry the whole burden, and in many cases their actuarial bases have been shaken if not destroyed. The number of workers covered by compulsory insurance schemes has been estimated by the International Labour Office as over 38 millions, with a further three and a half millions covered by voluntary schemes.² The variety of these schemes in the seventeen countries in which they are in force is too great to be summarised briefly; but, in general, the funds are derived from contributory systems in which the State subsidises the contributions of workers and employers. The increased payments caused by the depression, together with shrunken receipts, have necessitated an increase in State subsidies or advances in most compulsory insurance schemes. Some budgetary relief has been gained in certain countries by cutting down the rates of benefit and tightening the administrative regulations; but such relief has not been effective in making the schemes self-supporting and a great part of the economy gained is balanced by increased relief expenditure.

Despite the strain thrown on the funds and the heavy burden of supplementary relief, the principle, not only of unemployment, but of other forms of social insurance is stoutly defended and

¹ Pages 105-108.

² International Labour Office, "Unemployment Insurance and Various Forms of Relief for the Unemployed", Geneva, 1933.

seems to have won ground — for example, in the United States. “The State of Wisconsin has already adopted legislation for this purpose, and it seems certain that more comprehensive legislation will be initiated in the near future.”¹

In addition to the payments from insurance funds, however, the costs of relieving unemployment have mounted very rapidly. “In the United Kingdom, expenditure out of the unemployment fund was £51 million during the year 1924-25, of which 28.3 per cent was contributed by the State. In 1931-32, the total had risen to £120 million, of which 72 per cent was contributed by the State, these sums being in addition to the heavy burden carried by the local authorities. In Germany, RM. 1,071 million were spent on unemployment relief in 1928 (exclusive of local relief), of which only a small proportion was borne by the Federal and State Governments.² In 1931, the figure had risen to 2,338 millions, of which 38 per cent was borne by the Federal and State Governments. In France, 652.5 million French francs were distributed by the public unemployment funds in the period April 1st, 1931, to August 1st, 1932, of which 400 million francs were met by the State, the remainder being borne by local authorities. In the Netherlands, unemployment expenditure, which was 5.2 million florins in 1924, had risen to 24.9 million florins in 1931, of which 32 per cent was borne by the Government.³ In Switzerland, 1.6 million francs were spent in 1924, and 37.9 millions in 1931, of which 84 per cent was borne by the public authorities, including the communes. With regard to the United States, no accurate figures are available, but some idea of the amount expended on relief is indicated by an estimate made by the Children's Bureau of the United States Department of Labour,⁴ from which it appears that over 50 million dollars were spent during the single month of September 1932 in the areas for which statistics are available. This is not, however, by any means a complete survey.”⁵

As a further illustration of the immense scale upon which relief expenditure has been necessary in the United States, reference may be made to the distribution of commodity stocks.

¹ Report of the Director of the International Labour Office, June 1933. Cf. also C. M. BOOKMAN, “The Social Consequences and Treatment of Unemployment”, Presidential Address to the National Conference of Social Work, Philadelphia, U.S.A., published by the University of Chicago Press, 1932.

² About 20 per cent.

³ In addition to the 32 per cent chargeable to the communes.

⁴ *Monthly Relief Bulletin*, Vol. II, No. 3, November 1932.

⁵ Report of the Director of the International Labour Office, June 1933.

The Chairman of the Committee on Banking and Currency of the United States House of Representatives has stated that the total relief expenditure during 1932 by Federal State and local agencies reached \$1,000 million. (“Unemployment Insurance and Various Forms of Relief for the Unemployed”, Supplementary Report, page 14.)

During 1932, a total of 829,000 bales (414½ million pounds) of cotton and 85,000,000 bushels of wheat were released from Government stocks for distribution by the Red Cross. The distribution was carried through on a barter basis, millers and manufacturers handling the processing at cost and receiving payment in kind. ¹

To such direct relief payments must be added the increasing sums spent in a number of countries upon public works designed primarily to relieve unemployment and the many varieties of labour service, land settlement and small allotment schemes that have been carried out. In New Zealand, the Government has furnished aid to gold prospectors; in the United States, one of the first acts of the Roosevelt administration was the initiation of large-scale afforestation projects; in Germany, besides the tax-remission scheme launched by the von Papen Government, more than 500,000 persons have benefited from small-holding and allotment schemes.

It is difficult to judge the effectiveness of such relief. Not only is the increasing cost a heavy drain upon the budgets of national and local Governments (and also upon private charity), eating up resources that might under happier circumstances be available for the extension of more efficient production, but it seems clear that even such vast expenditures are not really adequate to relieve the distress occasioned by lack of work. In the presidential address to the National Conference of Social Work, previously quoted, it was estimated that the total amount of relief expenditure in the United States in 1931 was about 450 million dollars but, Mr. Bookman added,

“ Huge as this sum of 450 millions may seem when viewed by itself, or as compared with relief during prosperous periods, it is only about 2 per cent of the 22,000 millions estimated loss to all wage and salaried earners in 1931 and less than 5 per cent of the loss suffered by wage-earners alone engaged in the leading industrial occupations. ” ²

While it may be conceded that the disorganisation of industry and agriculture has been greater, and the facilities for relief have been less adequate, in the United States than in many other countries, there is an alarming volume of evidence concerning the growing social costs of the depression. A survey of mortality and morbidity statistics made by the Health Section of the League of Nations ³ appeared to indicate that, while there was

¹ “ Mass Relief in the U.S.A. ”, *London Times*, April 17th, 1933.

² “ National Conference on Social Work ”, *op. cit.*, page 7.

³ “ The Economic Depression and Public Health ” (document A.11(1).1932).

no noticeable increase of mortality rates to the end of 1931, there were not wanting indications even then that the general lowering of living standards, and underfeeding in particular, were beginning "to constitute a danger to public health". That such indications had not appeared sooner and in more startling form is a striking tribute to the greater efficacy of relief measures in the present crisis.

During 1932, the situation has become noticeably worse. Reports of medical health officers and school authorities, conferences of social workers, the publications of relief agencies, and official investigations of conditions among the unemployed bear witness to increasing sickness, stunted growth, and nervous strain, particularly among children and adolescents.¹ It is evident that the prolongation of unemployment and the general lowering of living standards have reached the point in some countries where they are not only sapping the vocational and moral efficiency, but are seriously undermining the physical stamina of millions of children and young people. The renewed efforts of public and private agencies to foster substitute occupations and healthy recreation, as well as to provide at least a minimum standard of food and clothing, admirable and deserving of all praise as they are, remain a poor substitute for the healthy exercise of individual initiative and responsibility in normal occupations.

THE MOVEMENT TOWARDS A REDUCTION OF HOURS OF WORK.

The prevalence and persistence of unemployment has naturally directed attention to a great variety of proposals, both of a palliative and of a remedial nature, aimed, not only at mitigating distress among the unemployed, but at finding a solution of unemployment. Until recent months the majority of such proposals were concentrated upon efforts in various ways to increase the demand for labour. Thus, most of the expert proposals put forward in preparation for the Monetary and Economic Conference have been designed to effect a restoration of trade and of monetary stability in order to revive production and exchange. In the same way, the schemes put forward in many quarters for public works expenditure, accompanied usually by plans for credit expansion, and the palliative schemes such as land allotments briefly referred to in the preceding section,

¹ Cf., e.g., "National Conference of Social Work", *op. cit.*, pages 126-135, 309-314. "Children, Young People and Unemployment". Save the Children International Union, Geneva, 1933; Part I — Germany, U.S.A., Belgium, Switzerland; Part II — Austria, Great Britain, Poland, etc.

have started from the idea of increasing the demand for labour. It has already been argued, however, and it is now generally admitted, that, even when the present crisis is surmounted, there will in all probability remain "a hard core of unemployment", if only because of the displacement of labour by reason of the rapid improvement of industrial technique. In these circumstances, it is not surprising to find that a strong movement has developed in the direction of controlling the supply of labour, while at the same time stimulating demand for it.

This movement takes many forms, such as the elimination of married women from certain forms of employment, the objections raised to double employment, measures to raise the school-leaving age, and lowering the age of retirement, that amount in the aggregate to a considerable restriction of the labour supply, but are impossible to measure statistically. For the most part they are the result of private initiative or social pressure exercised in specific industries or localities.

The movement towards a reduction of working hours, which is the most important manifestation of the attack on unemployment from the side of labour supply, has developed considerable strength in recent months both by actual application in specific cases and by public discussion of the possibilities of international action. Historically, it is a continuation of the tendency towards a limitation of working hours which has been a characteristic accompaniment of the introduction of machine methods in industry. Ever since the first factory Acts were passed in England regulating the employment of children and young persons, there has been a continuous extension of the principle. Not only the age at which employment is permissible, but the number of working hours in the day, the times during which work is permitted, rest-periods and holidays, have been prescribed for adults as well as children, as much by public opinion and, in recent years, by business initiative, as by actual legislation. The persistent tendency has been to restrict the supply of labour by regulations and practices which limit the duration of effort on the part of the individual. Forced into operation at first by the humanitarian pressure of public opinion, often upon reluctant employers, such regulations have, on the whole, been later justified upon purely economic grounds. Increased efficiency of labour, improved management rendered necessary by the restrictions placed upon labour supply, together with an increased use of capital equipment and a stimulation of labour-saving inventions, have accompanied, if they have not been wholly caused by, the limitation of working hours and rising standards of living.

The more recent acceleration of the industrial revolution, and particularly the rapid development of mass-production

methods by the utilisation of automatic machines, together with the improved management which has come to be known as rationalisation, have brought possibilities of further reductions in the working day and the working week. It is significant that, in the post-war period, the initiative in reduction has come not so much from the workers, or from public opinion, as from those employers who have gone furthest in introducing the new machine methods of production. The shorter working week, accompanied usually by higher wage-rates, has been introduced by such employers in advance of legislation. The standard of legislation even in the more advanced countries, in this respect, remains the eight-hour day. This was an aspiration of the Chartist movement, put into force in 1848 by one of the New Zealand group settlements, and later established as a general practice in the Australian colonies and in New Zealand. It has for at least a generation been the recognised standard of advanced industrial countries and, since the first International Labour Conference in 1919 drafted the Eight Hours Convention, has been the goal of international regulation also.

In the post-war period, however, while the efforts of labour leaders and social reformers were largely directed to securing an extension and consolidation of the eight-hour day, and the forty-four- or forty-eight-hour week, certain highly mechanised industries, or even single establishments, introduced an even shorter working week. The motives which led to this action, and the circumstances which made it possible, were economic rather than humanitarian. Up till the present time such a reduction has been attempted only in a few specific industries, notably the production of motor-cars, in which mass-production methods were particularly suitable and which also enjoyed unusually rapid growth and expanding prosperity in the exploitation of hitherto unsatisfied demands.

Both the reduced hours and the higher wages characteristic of such industries have been justified as providing the leisure and the purchasing power necessary to sustain demand among the workers for the products of the new industries ; but, in fact, the primary reason which made possible shorter hours, higher wages and greater purchasing power was the enormously increased efficiency of production by the new methods. While in the past, when the labourer's skill was relatively a more important factor in production, shorter working hours undoubtedly resulted in improved efficiency and greater production, the predominance of the machine in modern industry has thrown initiative in this respect rather upon the management than upon the workers and reduced hours have been the result rather than

the cause of greater efficiency and increased production. There is every reason to expect that continued, and accelerated, technical progress will extend the possibilities of such reforms over a wider and wider area of production, but the fact must not be overlooked that technical progress depends, not only upon scientific inventions, but also upon the commercial possibilities of utilising such inventions and particularly upon the supply of real capital made available by community savings. A period of rapid credit expansion, in which capital investment runs ahead of savings, is particularly stimulating to those industries which are most likely to utilise new scientific methods and therefore to embark upon the more advanced labour standards. But the nemesis of such a period is an unbalancing of production which inevitably results in a financial crisis, as a result of which the labourers as a class lose infinitely more in unemployment than the fortunate workers in the expanded industries had gained in improved standards.

While it is not possible upon any but experimental grounds to determine at any moment what is the precise degree to which increased productive efficiency warrants the raising of living standards and the shortening of working hours, it is important to distinguish between such improvements as are definitely warranted by such increased efficiency and proposals for raising standards as a means of overcoming financial crisis and economic depression. There is general agreement concerning the wisdom and necessity of allowing increased productive efficiency to be reflected in rising standards, but there is a sharp conflict of opinion concerning the possibility of taking action in circumstances such as the present.

There is an impressive number of instances in which, especially during 1932, and mainly as a result of the initiative of certain groups of employers, working hours have been reduced, generally as a means of spreading available employment. In the majority of cases, such reductions have been accompanied by proportionate decreases in weekly earnings; but in some instances the same wages are being paid for the shorter working time.¹ Whether such reductions of hours as have been accompanied by the maintenance of earnings will prove tenable must be left to the future. It is possible that, in some cases, they represent a belated recognition of the advances made possible by improved efficiency.

The logical culmination of such a movement, with its mixed background of improved technical efficiency, persistent and

¹ Cf. the survey made by the International Labour Office, "Hours of Work and Unemployment", Chapter IV.

costly unemployment, and economic and financial theories advocating the maintenance of consumers' purchasing power, is to be found in the effort to establish by legislative action a more or less uniform shorter working week. The most important national efforts in this direction were the introduction into the United States Congress of a Bill designed to establish a thirty-hour week in industry and the definite action in this respect taken by the German Government in June 1931.¹ The American measure was based upon a recommendation of the President's Committee upon Unemployment, which gave rise to a widespread "share the work" movement fostered, *inter alia*, by the Federal Reserve Bank system. The German measure, referred to above, was also quite definitely designed to share available employment and was accompanied by wage reductions. The international movement naturally took place under the auspices of the International Labour Organisation, whose publications contain the most adequate summaries so far published of the extent to which reduction of hours has been carried up to the present, and of the arguments for and against its consolidation and extension by means of international agreement.²

A survey of the literature of this subject reveals the necessity of separating the three main elements of the movement towards shorter hours. Concerning the first, the necessity of allowing increased technical efficiency to be registered in improved working conditions, there is general agreement. While it is possible to exaggerate the degree to which technical progress has been made in industry as a whole, rather than in particular industries under the stimulus of boom conditions, it is a commonplace that the pace of progress has been accelerated in recent years. Most students of the subject would agree that, apart from the unemployment caused by the present breakdown of industry and trade, there is a more persistent problem of unemployment largely caused by structural changes in industry and by the rapidity with which labour-saving devices have been introduced. Geographical shifts in the localisation of industry cannot be combated by shorter hours; but unemployment caused by improved efficiency of production is generally agreed to warrant a reduction, and it is certain that, when the immediate crisis is past, the movement towards shorter hours will be accelerated.

The use of a shorter working day or week as a means of spreading employment at the present time also commands a con-

¹ Cf. the survey made by the International Labour Office, "Hours of Work and Unemployment", pages 72-76.

² Cf. especially the memorandum published by the International Labour Office under the title "Hours of Work and Unemployment", Geneva 1933; the discussions of the Preparatory Conference in January 1933, and the convenient summary analysis of these discussions by M. Fernand MAURETTE in the *International Labour Review*, March 1933.

siderable measure of agreement, and most of the instances of reduction recorded seem, in fact, to be prompted largely by this motive. The demoralising effect of continued unemployment, especially when it is concentrated upon the less fortunate workers while those in full employment enjoy higher standards of real wages, is too obvious to need elaboration. The crucial point upon which opinion is sharply divided, however, is whether such a spreading of the available work should be accompanied by a reduction in earnings.

This division of opinion, clearly illustrated in the discussions at the Preparatory Conference organised by the International Labour Office in January 1933, depends fundamentally upon, and is best considered in connection with, the conflicting views held regarding the restoration of consumers' purchasing power as a means of escaping from the present economic depression. Before describing this conflict of opinion, however, reference should be made to certain practical difficulties involved in establishing general principles for the reduction of working hours. Such difficulties in applying a general rule are not new, except perhaps in their international scope. Every proposal for legislation to raise labour standards has encountered such problems as those presented by the smaller, less efficiently organised industries — the necessity of adapting management to the new conditions, and the disturbance of equilibrium between labour costs, capital costs and selling prices. Such problems, however, if the desirability of the reform be granted, have never proved, and are not likely now to prove, insoluble. Even when to industrial differentiation there is added the more difficult problem of international competition between countries at different stages of economic development, there are clear possibilities of administrative adjustment — such, for example, as the suggestion made by the Danish and Swiss Governments' representatives at the Preparatory Conference for regulation by groups of industries.

The real crux of the problem, to which the Preparatory Conference discussions led from every angle, is the division of opinion concerning the wisdom of pressing ahead with such a reform in the midst of a depression. It is clear that any arrangement, even of a temporary character designed to spread work, is likely to become permanent, especially if it is not accompanied by wage reductions. Whether such a definite raising of living standards, involving the probability of some increase in labour costs of production, is opportune at the present time is the real issue of the debate. There is, however, more involved in the discussion than variant opinions concerning the extent to which industrial progress has, in fact, made possible and even necessary a shortening of hours. The reduction of hours accompanied by the maintenance of wages is, in addition, advocated as an

immediate practical way of escape from the crisis on the ground that it will extend consumers' purchasing power and thereby increase demand.

At this point there arises in another form the fundamental divergence of views concerning the nature of the economic and financial breakdown which has been discussed already from many other angles. Those who advocate measures to increase consumers' purchasing power base their proposals upon the theory that the crisis arose because of a failure of purchasing power to keep pace with the increase of productive capacity during the preceding boom. The opponents of this view, while not denying that such a development may occur in the final stages of an investment boom, and be followed by a collapse of purchasing power in the ensuing depression, maintain that the fundamental error of the expansion period was a misdirection of capital resources and over-investment relative to savings. In the latter view, it becomes a primary necessity, in the depression, to liquidate past capital losses and so adjust the costs of production as to make possible again the accumulation of real capital resources out of the restored profits of industry. Measures which would have the effect of increasing labour costs are, in this view, calculated to retard rather than hasten recovery from the depression.

The theoretical problem of the effects likely to be produced in more normal circumstances by a reduction of hours and rising wage-levels can be stated only in tentative, hypothetical terms. Such a change in the supply, and therefore in the price, of labour disturbs the balance between labour and capital costs and between costs in general and demand prices. Where the new equilibrium will finally settle depends upon a number of independently variable factors, such as the changes induced in labour and management efficiency, in the supply of capital, and the rate of interest, as well as in the reactions of consumers' demand.

The practical question, therefore, comes back to the wisdom or unwisdom of launching an advance in labour standards, involving at least temporarily and in certain industries an increase in labour costs. At the moment of writing, in the spring of 1933, the controversy is unresolved and action is suspended. Meantime, events march rapidly in other directions and monetary fluctuations involving fresh and disconcerting disturbances of existing price disequilibria in almost every direction are changing the whole setting of the problem.

Chapter V.

THE PROFITS OF ENTERPRISE.

THE CAPITAL MARKET.

The preceding chapters devoted to production and prices have clearly shown a very great shrinkage of national incomes since the depression began. Other chapters demonstrate the difficulty of maintaining wages and governmental expenditure at their pre-depression levels. In the present chapter, attention is directed to what is often described as the "residual" share in the national income, the profits of business and financial enterprise. It will be shown that business earnings have declined very heavily, so that actual profits have in many important instances been turned into substantial losses, especially during 1932. At the same time, it is clear that, during the early stages of the depression, a general attempt was made to maintain dividends, even though earnings had seriously declined. The maintenance of wage-rates, dividend payments, debt service and governmental expenditures in face of shrunken national incomes, however, was rendered possible only by drawing upon or failing to replenish capital reserves.¹ As the depression persisted it

¹ *E.g.*, in Germany, the annual investments in fixed capital and stocks have been estimated as follows in RM. (000,000,000's).

Year	Fixed capital (Anlagen) Net investment	Stocks (Lager) Net investment
1924	2.7	5.5
1925	4.5	2.7
1926	5.2	— 2.4
1927	7.2	4.1
1928	7.3	2.7
1929	6.1	— 1.0
1930	4.0*	— 3.9*
1931	—	— 5.0*
1932	— 3.0*	...

Vierteljahrshefte zur Konjunkturforschung, VII, 4. Teil, A. (Sonderheft zur *Konjunkturforschung* 32). *Konjunktur-Statistisches Handbuch*, 1933.

* Provisional.

became clear that there was proceeding a distributive struggle of profound significance, and that upon the issue of this struggle depended the possibility of replenishing capital resources. The pages which follow are devoted to various aspects of this double problem.

The growth and ramification of the capital markets in highly developed financial communities has been very rapid in recent years. The processes by which capital is heaped up through the collection of small and large amounts from different sources and redistributed into the many and diverse channels of investments are complex and intricate. The small capitalist who, by severe economy, accumulates a balance in his savings-bank account, the building society member who pays small regular contributions, the policyholder who makes his savings by paying insurance premiums, all play a part, individually negligible perhaps, but of great aggregate significance in the supply of capital. Their savings are reinforced by the reserves set aside by great corporate enterprises, and the whole fund of capital contributed from these and many other diverse sources is distributed to a multiplicity of borrowers ranging from Governments to small private enterprises and individuals by the operations of many different types of financial institutions.

The liquid medium through which this continuous but complicated process of accumulation and redistribution takes place is credit. The lender, whether he is a child depositing pennies in a savings bank or the director of a large enterprise determining the proportion of net earnings which will be placed to reserve, takes a decision which, directly or indirectly, gives over to another person the purchasing power which might be used by him for immediate consumption. The command over real resources — goods and services — is transferred from lenders to borrowers.

The whole process, however, is complicated by the fact that it becomes merged with, and in practice indistinguishable from, the process by which all payments are made. The modern credit system, in providing a means whereby goods and services are exchanged, provides at the same time the means whereby resources are transferred from lenders to borrowers.

Credit however is, and must be, managed and directed by human intelligence. In the last resort, it depends upon nothing more than faith or confidence that the resources, or the titles to resources, which are entrusted to another person or institution will be repaid in accordance with the contract entered into. The complexity of modern transactions has created the necessity for specialised financial institutions to judge and interpret, not only the credit-worthiness of individual transactions, but

the demand and supply of credit in the community as a whole.

The extent to which these financial institutions occupy a dominating position in the present economic system depends, not only on their actual size, but also upon their influence on all other economic enterprises. Their size may be judged by the following statistical estimates. In the United States, the capital invested in financial institutions was registered in 1929 as approximately 26 per cent of the total capital invested in corporate enterprises; their income was about 20 per cent of the total corporate income, while their liabilities were over 40 per cent of the total liabilities of all corporations.¹ In Germany, in 1928-29, their capital was about 20 per cent, income about 22 per cent, and public liabilities over 60 per cent of the total.² In Italy, their capital was in 1930 about 15 per cent of the total capital of all companies and their public liabilities about 60 per cent of all companies.³ These statistics, while subject to a liberal margin of error, indicate how large a proportion of the resources and activities of a modern community are engaged in the financing of industry and commerce.

Because of their intrinsic importance as large-scale institutions, the financial structure of these great financial enterprises deserves separate examination. In themselves, they constitute an important channel of investment, and decisions in regard to their capital structure, dividends and reserve policies bulk large in the determination of financial policies in the economic system as a whole, apart altogether from the influence they exert upon other forms of investment. Fairly complete statistics are available for a number of countries as far as the most important financial institutions — the commercial banks — are concerned. These are summarised in the League of Nations *Memorandum on Commercial Banks, 1913-1929*.⁴

Attention was drawn in the *World Economic Survey, 1931-32*, to some of the important changes in the banking situation after the war.⁵ There was, *inter alia*, a strong tendency in many countries for the liabilities of the banks to increase at a faster rate than the increase in their capital.⁶ This was the case, for example, in such countries as Austria and Germany, where post-war reconstruction was financed largely by international

¹ Cf. United States Treasury Department, *Statistics of Income, 1929*, pages 332-337.

² Cf. *Vierteljahrshefte zur Statistik des Deutschen Reichs, 1930, II*, page 72 (only companies with a capital of at least a million RM. share capital or shares quoted on the Stock Exchange included).

³ Società Italiane per Azione, *Notizie Statistiche 1932*, pages 19 and 20.

⁴ 1931. II. A. 26. A new edition, covering the years 1925-1933, will be issued at the end of 1933.

⁵ *World Economic Survey, 1931-32*, Chapter VII.

⁶ *Ibid.*, page 207, and *Commercial Banks, 1913-1929*, page 26.

loans, which reached industry through the banks. But there was, in the period of war inflation, a general tendency for the proportion of capital to liabilities to be lowered, and this tendency persisted in many countries after currency stabilisation had been achieved. In the later stages of inflation, many enterprises accumulated large hidden reserves, and these were transferred again to capital account after the currencies had been stabilised. After this readjustment, however, the proportion of capital to turnover began in many countries to decline again. In almost every country the proportion remained considerably lower in 1929 than it had been in 1913. This was a natural continuation of the well-recognised tendency, even before the war, for the volume of credit to expand relatively to the capital of the financial institutions. There is an increasing complication of exchange in modern economic life and some part of the apparent increase is due to the multiplication of transactions; but the relatively more slender capital basis upon which these transactions were conducted rendered the banking systems of many countries more vulnerable in the event of major shocks to credit, such as, in fact, occurred in 1929 and the following years.

While the expansion of credit before 1929 was greater than the increase of banking capital, there was in most countries a substantial increase in that capital. In those countries which had suffered currency inflation, there were losses of banking capital which were only partially restored after stabilisation. Thus, in Germany, Austria, Hungary and France, bank capital was less in 1929 than in 1913. In all other countries for which information is available, except the Argentine, commercial banking capital and reserves have been increased above the pre-war amount. The increased vulnerability referred to in the previous paragraph was therefore caused by the credit expansion, not by a shrinkage of capital.¹

There is evidence also of a considerable growth in many countries of other types of financial institutions. Among these may be mentioned the investment trusts in the United States, to which attention was drawn in the *Survey* for 1931-32.² The total capitalisation of the investment trusts in the United States rose from \$15 million in 1923 to \$3,990 million in 1929. The rapid development of investment trusts and the high rates of profit earned by them, largely from sales of securities that had appreciated, was a considerable factor in the speculative boom in the United States.³

¹ *Commercial Banks, 1913-1929*, page 28.

² Pages 54-5.

³ Cf. Joseph A. Thomas, "Ten Investment Trusts in America; a Three-Year Record", *Harvard Business Review*, October, 1930.

Moreover, there was a distinct tendency — measurable in the United States — for the profits of financial enterprises to increase faster than those of industrial enterprises. The incomes of manufacturing corporations in that country increased at an annual rate of 5.3 per cent in the boom period, and that of trading enterprises fell by 0.2 per cent, while construction and public utility corporations showed an annual gain of 10 per cent and financial institutions a gain of 16 per cent.¹ This higher rate of increase was shared by all the principal forms of financial enterprise — commercial banks, savings banks, loan and trust companies, stock brokers, real estate companies and insurance firms. There was, however, a very high casualty rate among these enterprises, giving evidence of a speculative market.

It is, however, mainly in respect of their influence upon credit, and thereby upon the capital market in general, that financial institutions in the post-war period contributed to the disequilibrium that arose between the actual earnings, and therefore the new savings of industry, and the burden of capital charges that industry had to carry.

Speculation and the growth of financial institutions were most marked perhaps in the United States; but the same tendencies were evident in many other countries during the period before 1929. Attention has been drawn to this tendency in a previous publication of the League of Nations² and is referred to in another connection later.

There are not, and cannot be, in the constant flux of human activity that makes up the economic system, any set and invariable rules by which those who direct these specialised institutions — bankers, brokers, financial middlemen of all kinds — may be sure in advance that their judgment and estimates of the credit situation will be accurate. On the contrary, the money market is so organised as to provide for the play of interacting, competitive forces, which, by a continuously corrected process of trial and error, keeps the demand and supply, and the prices, of the various forms of credit in fairly stable if shifting equilibrium.

It is not surprising, therefore, to find that the actions of financial institutions in estimating the credit needs of the community must often be reckoned an active rather than a passive factor, influencing not only the means of payment in general, but also the supply and demand of capital. It is often said that, in an ideal society, the supply of monetary means of payment should be kept "neutral" and should be governed

¹ F. C. Mills, "Economic Tendencies in the United States", New York 1932, pages 482-485.

² *Commercial Banks, 1913-1929*, page 14.

by the demands for it set up by economic transactions. But such an ideal is never perfectly achieved, and errors of estimation and judgment are often cumulative. The consequences have been aptly described as resembling a chemical reaction which "proceeds regularly while the temperature of the medium in which it is immersed remains constant, but quickens when the temperature rises and slackens when it falls. So the operations of the Money Market, immersed as it were in a medium of credit, proceed regularly when the level of credit is normal, quicken as this level rises and slacken when it falls."¹

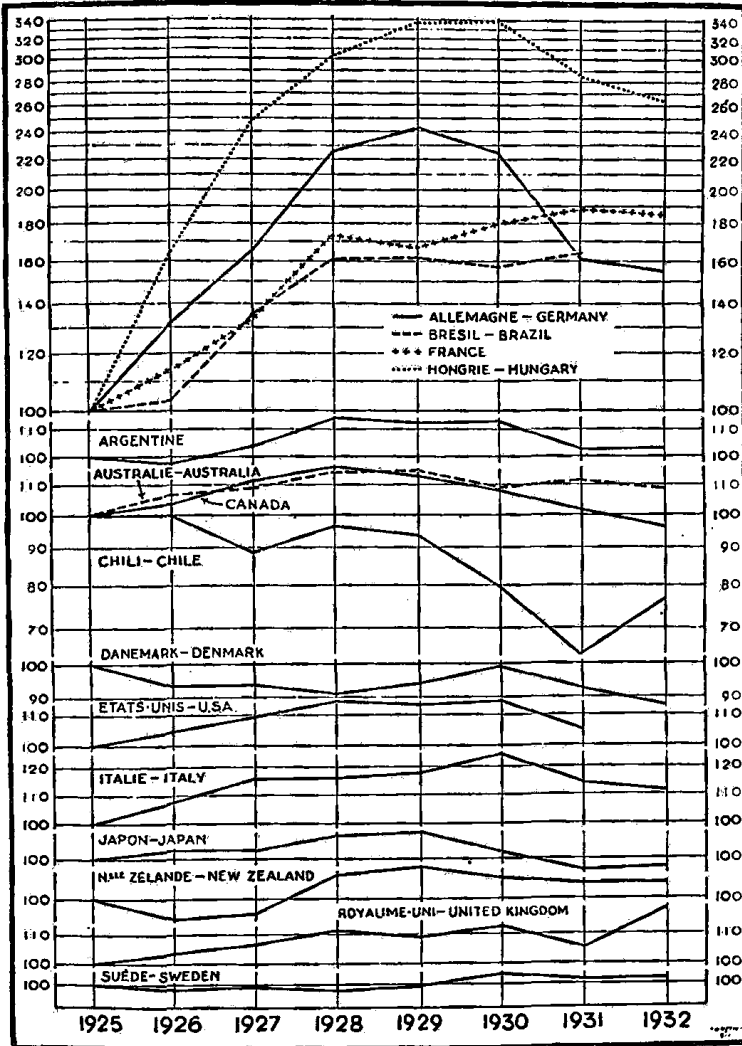
This influence of the supply of credit upon the relationships between savings and investment is particularly important in such periods as that from 1925 to 1929, when there was a great expansion of credit in practically every country of the world. It was equally important in the years following 1929, when the supply of credit contracted violently and cumulatively in most countries.

In the language used above, both the level and the temperature of the credit stream were rising almost continuously from 1925 to 1929, and both have been falling rapidly since 1929. In other words, the amount of credit made available in the world's money markets offered favourable opportunities to borrowers in the former period and tended to discourage them in the latter. Such a broad statement, however, needs a very great deal of qualification before it fits the actual circumstances. Perhaps the best measure of the volume of credit made available in these years is found in the deposits of the commercial banks. While most countries shared in the growth of deposits before 1929, the increase was most marked in those which were most engaged in international lending and borrowing. The United States, among creditor countries, and Germany, among the debtors, are outstanding examples; but, as the accompanying diagram shows, the tendency to increase was widespread.

Comparison of the total amounts of bank deposits at different periods, however, only tells part of the story. The rapidity with which these deposits were turned over, or, in economic language, the velocity of circulation, multiplies their effectiveness. In periods of expanding credit and active business, the velocity of circulation increases, so that a given volume of credit changes hands more often and is therefore capable of financing a greater number of transactions. The variations in the velocity of credit transactions have been measured in the United States, and the calculations show that the annual turnover of accounts, which

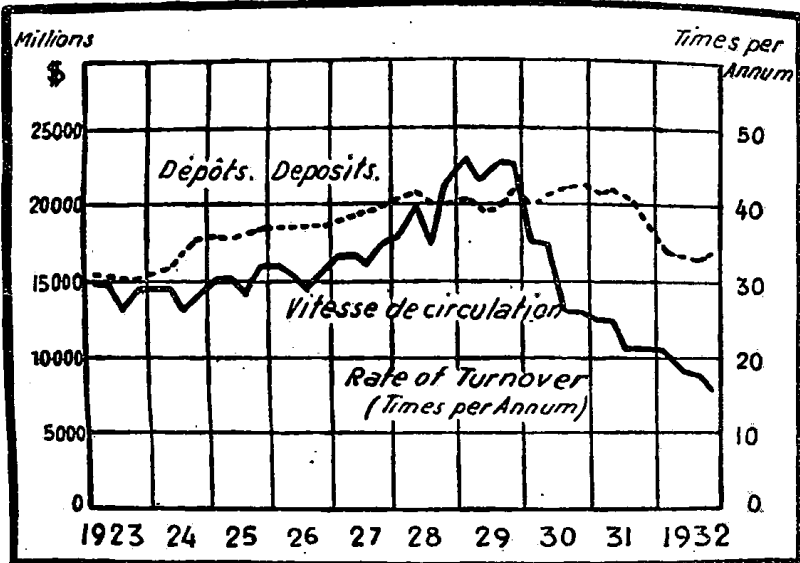
¹ F. Lavington, "The English Capital Market", London, Methuen, 1921, page 21.

Commercial Bank Deposits, 1925-1932.
(At the End of Year.)
(1925 = 100).



was between 26 and 32 times per year in 1923-1925, rose steadily, till, by October 1929, it was 45 times per year. In 1930, the figure fell abruptly to 26, and continued to fall till, in the last quarter of 1932, it was only 16. The fluctuations are summarised in the following diagram.

*Deposits and Rate of Turnover of Reporting Member Banks in Leading American Cities.*¹



These statistics indicate how large a part fluctuations in the velocity of circulation played in the expansion before 1929, and equally in the contraction of the following years. Their effect in swelling the total volume of credit transactions, particularly in the years 1927-1929, was illustrated in the *Survey* for 1931-32 by a diagram which showed that transactions increased by over 60 per cent from the beginning of 1927 to the peak in October 1929, while the net deposits of the banks which were members of the Federal Reserve system did not increase more than 6 per cent. The most recent calculation available illustrates the enormous contraction of transactions since 1929. "Between 1929 and 1932 the total decrease in debits to individual accounts may be estimated at more than \$700,000 million, or 70 per cent, of which two-thirds represents a decline in debits at banks in

¹ *Federal Reserve Bulletin*, January 1933, pages 4 and 5.

New York City. The greater part of this decline in New York reflects a decrease in the volume of security transactions and a sharp decline in security prices. Developments in the security markets have also been an important factor in the decline of debits at banks outside New York City, but at these banks changes in the total volume of money payments have been affected in an important degree by decreases in business activity and lower levels of prices and wages.”¹

There seems little doubt that, not only in the United States and in certain borrowing countries where the evidence is equally clear, but in practically all countries, the expansion of credit, bearing in mind local circumstances, was greater than the actual growth of industry. A tabular statement in the *Survey for 1931-32*,² shows that, even when allowance was made for price changes, the deposits of commercial banks increased in the years 1925-1929 by percentages ranging from 17 per cent in the case of Sweden to 104 per cent in Germany. When it is remembered that the velocity of circulation also increased in this period, it is clear that the increase of credit transactions in many countries was much greater than that of population, production or trade.³

The most important effects of such credit expansion are to be found in a distortion of productive organisation. The increased credit available draws real resources from one use to another. Not all industries and occupations and, in these days of international borrowing, not all countries advance at the same pace. It may be shown that, between 1922 and 1929, industrial production in the United States increased faster than the burden of domestic debt; but such a statement needs to be supplemented by such facts as those relating to American loans to countries where debt increased faster than production, and by reference also to the irregularity of the industrial advance within the United States, as well as to the great speculative market in securities and real estate which developed in this period.

An examination of the assets side of banking balance-sheets shows a clear tendency towards a weakening of the distinction between pure deposit banking and investment banking. There was also an increased creation of new financial institutions such as financial trust and holding companies. “Such companies have experienced a marked development in recent years, both in the countries where industrial banking is most characteristic and in those where deposit banking still predominates.”⁴

¹ *Federal Reserve Bulletin*, January 1933, pages 4-5.

² Page 209. For the increase in production and trade, see also *World Economic Survey, 1931-32, passim*.

³ *Federal Reserve Bulletin*, January 1933.

⁴ *Commercial Banks, 1913-1929*, page 14.

A great part of the credit expansion, in other words, was not devoted to financing a growing volume of production and trade, though such a growth did account for some of the additional credit issued. It was devoted to creating new financial institutions and to speculation in industrial and financial securities and real estate. The index-numbers of security prices in this period show movements out of relation to the much slower increase in production and trade.

Index-Number of Stock Exchange Security Prices.
(Average of Years.)
(Base : 1925 = 100.)

Country	1925	1926	1927	1928	1929
Germany	100	113.2	165.3	152.6	135.2
Austria	100	95.4	116.5	112.8	103.1
Canada	100	131.9	173.6	245.5	352.2
United States	100	113.1	133.0	174.5	214.3
France	100	110.7	134.1	202.4	256.1
Netherlands	100	100.0	111.8	122.6	125.8
Poland	100	61.9	149.7	157.6	104.7
United Kingdom	100	105.5	113.8	130.3	127.5
Switzerland	100	120.5	145.4	178.5	170.3
Czechoslovakia	100	90.9	113.6	161.4	162.5

There is little need to give further evidence of widespread speculation in securities and real estate during the boom period. The instability which resulted from the heavier nominal burden of ownership claims thus loaded upon the world's productive organisation has become a matter of history. A later section of this chapter is devoted to a summary description of the manner in which these exaggerated property claims have broken down the productive mechanism and have finally recoiled in many cases upon the banking and currency systems of the countries concerned.

INDUSTRIAL FINANCE BEFORE THE DEPRESSION:

It has been shown that, in some countries, prior to 1929 the capital market was stimulated to an almost feverish activity by the prevailing credit conditions. Much of the increased credit made available went to support a speculative boom in real estate and securities. Some of it went also to the expansion of financial enterprises. As in all such periods, however, the abundance of credit also stimulated industrial investment. There was, after the pacification and stabilising of Europe in the early 'twenties, a genuine economic revival based upon the

demands for reconstruction, and this would in any case have led to increased industrial investment and a period of active business. An immense extension of international lending, together with domestic speculation in many countries, both facilitated by a cheapening of certain forms of credit, exaggerated the revival of 1925-1929 into a reconstruction boom. In the course of that boom there was a considerable distortion of industrial investment and probably, in the aggregate, over-investment relatively to the world's savings. While the total over-investment cannot, in the present state of statistical knowledge, be precisely demonstrated, there is little doubt that in many countries, and in many industries, investment was pushed to such lengths as seriously to disturb the balance of industrial development. The inevitable result was a derangement of prices leading to a persistently falling price-level and a prolonged period of depression in which the necessity of re-valuing the investments of the boom period became more and more imperative.

In the present section an attempt is made to analyse, and to give statistical illustrations of, the financial policies of business enterprises in the years preceding the depression. The material used is drawn as far as possible from official sources. This material, however, is both fragmentary and difficult to interpret. Despite the advance in accounting methods and the general tendency for the taxation of corporate enterprises to increase, the published official statistics, both of the valuation and of the income of such enterprises, leave a great deal to be desired from the point of view of economic analysis. They may be supplemented to some extent by private investigations, particularly of business profits, which utilise the published balance-sheets of particular enterprises. Such private investigations are almost necessarily confined to comparatively small samples of the total of business activity within a country and, moreover, encounter great statistical difficulties in any attempt to establish a comparable series over a period of years. As increasing attention is directed by economists and statisticians to this fruitful field of research, some progress is being made in surmounting the technical difficulties presented by the available data;¹ but no amount of statistical ingenuity can overcome the fundamental difficulties arising from the incomplete, and sometimes inconclusive, nature of the information made available to the general public.

In the discussion which follows, no attempt is made to separate the various elements of which business profits are composed.

¹ Cf., e.g., Sir Josiah Stamp, "Industrial Profits in the Last Twenty Years: A New Index Number", *Journal of the Royal Statistical Society*, Vol. XCV, Part IV, 1932.

The statistics used are those of the net earnings of industrial and commercial corporations, excluding financial enterprises. Net earnings include the very important element of interest upon owned capital, as well as profits in the narrower economic sense of reward for undertaking risk. Essentially the profits of business enterprise, as measured by the available statistics, consist of the share of the product of industry taken to satisfy ownership as distinct from wage claims or payment for borrowed capital.

It must be recognised, also, that there are considerable variations, not only in the use of terms, but also in the actual financial structure and in accountancy methods, that render impossible exact comparisons between developments in different countries. Attention may be drawn, on the other hand, to significant tendencies which appear in more than one country.

The first broad generalisation which may be made is that in the years immediately preceding the depression there was a rapid increase in the value of the capital invested in corporate undertakings as measured by the statistics of paid-up capital, both preferred and ordinary, and of undivided profits carried to reserves. This may be illustrated by the following table.

*Growth of Owned Capital Invested in Corporate Business Enterprises, 1925-1929.*¹

Country	Unit	1925	1926	1927	1928	1929
United States	\$ (000,000,000's)	94	98	107	113	122
Italy	Lire (000,000,000's)	29	34	38	41	45
United Kingdom*	£ (000,000's)	880	980	980	1,060	1,080
Switzerland	Francs (000,000's)	2,779	2,733	2,829	2,920	3,057

While these figures show a general tendency to increase in the years 1925-1929, the rate of increase varies considerably from country to country. It is not possible to comment upon such variations, since the data is inadequate. Nor is it possible, in the absence of adequate information concerning the volume of savings in the various countries, to form a final opinion concerning the relation of investment to actual savings. There are, however, certain indications that point to the probability

¹ Owned capital defined as share capital plus reserves and balances carried forward, except in the case of Switzerland where the statistics are of share capital only.

United States: *Statistics of Income*.

Italy: Società Italiana per Azioni, *Notizie Statistiche*.

United Kingdom: Colin Clark: *The National Income, 1924-1931*.

Switzerland: *Annuaire Statistique de la Suisse, 1926-1930*.

* The statistics refer only to a selected sample of 700 industrial companies and therefore do not measure the aggregate growth of all companies. Statistics of the paid-up share capital of British joint-stock companies registered under the Companies Act, 1862, which includes financial joint-stock companies, are as follows: (£000,000's), (1925) 4,519, (1926) 4,686, (1927) 4,907, (1928) 5,027, (1929) 5,250.

that, in the post-war period as a whole, and especially in the years 1925-1929, important sources of savings decreased. This is clearest in the case of the so-called "automatic saving" of corporate enterprises. Under the pressure of heavy taxation, and of the changed nature of their capital obligations, these enterprises were not able to set aside reserves in the same proportions as before the war. This fact is illustrated in the following table, which includes financial as well as industrial enterprises. It will be clear that the proportion of earnings set aside as reserves fell between 1925 and 1929. Credit in certain forms was so plentiful in those years, especially in the United States, that it was more profitable for the companies to float new issues on the market than to set aside reserves from their own earnings in order to finance expansion of their enterprises.

Percentage of Industrial Profits Placed to Reserves.¹

Country	Average 1910-1914	1925	1926	1927	1928	1929
Germany ²	23	23	22	20	19	14
Italy		25	21	22	22	20
United Kingdom ³	26	22	21	17	22	19
United States		31	20	4	14	1

An attempt has been made in Germany to measure the proportion of such corporate savings both to the total net investment of new fixed capital (Neuanlagen) plus additions or decreases of stocks (Vorräterveränderung) and changes in gold reserves (Goldbestandveränderung) and to the national income. The results of this investigation are summarised in the table which follows :

Investment in Germany, 1924-1929.⁵
(RM., 000,000,000's).

	1924	1925	1926	1927	1928	1929
Net investment	8.5	7.7	3.3	11.3	10.8	4.6
Net capital imported from abroad	1.0	3.4	0.6	4.4	4.2	2.3
Net domestic investment	7.5	4.3	2.7	6.9	6.6	2.3
Undistributed company profits . .	...	0.9	0.9	1.3	1.3	0.8
National income . . . . .	...	60.0	62.7	70.8	75.4	76.1
Net domestic investments as a percentage of national income	...	7.2	3.7	9.7	8.8	3.0

¹ Germany: *Vierteljahrshefte zur Statistik*, 1911-1915, 1926-1930.
 Italy: *Società Italiana per Azione, Notizie Statistiche*, 1932.
 United Kingdom: *Economist*, Bank of England Statistical Summary, March 1932.
 United States: *Statistics of Income*, 1925-1929.
² Companies with a nominal capital above 1,000,000 RM. (about 85 per cent of total).
³ Insurance companies excluded.
⁴ No net savings.
⁵ Institut für Konjunkturforschung: *Sonderheft 22*, page 26; *Wochenbericht* 1932, No. 23, page 94. Statistisches Reichsamt, *Statistisches Jahrbuch für das deutsche Reich*, 1932, page 526.

A distinct rise is shown in the proportion of national income devoted to investment in the boom years 1927-1928, apart from the capital borrowed abroad. Of this new investment, however, a lower proportion was provided by the undistributed profits of the corporate enterprises themselves.¹

In the absence of adequate statistics concerning the various forms of savings and the manner in which such savings are invested,² it is not possible to support or criticise the widely held opinion that, in the boom years, investment proceeded at a faster rate than capital could be accumulated through the ordinary means of saving, and that a part of the investment was, in fact, made possible by credit inflation. The German estimates quoted above, however, draw attention to the great part played in the borrowing countries during the years before 1929 by international lending. A clear distinction needs to be drawn between the capital-exporting and the capital-importing countries. In the former, business indebtedness, while remaining high and increasing in some cases, did not increase as fast as the capital and reserves invested as equities. In such countries it was possible to finance the expansion of business by direct appeal to the capital market resulting in the flotation of new shares, or simply by using undivided profits. Thus, in the United Kingdom and in the United States, as will be evident from the following table, the proportion of indebtedness to capital fell on the whole between 1925 and 1929. This statement, however, needs some qualification in the case of the United States, where there was a marked increase in certain forms of business indebtedness after 1927 and where a change in banking policies facilitated the flotation of new issues by a large expansion of bank loans upon industrial securities. While not strictly a creditor country, Italy has been included in the first group, since industrial finance in that country in recent years has relied mainly on the domestic capital market,

¹ Colin Clark, "The National Income 1924-1931", London 1931, pages 63, 70, 138, gives the following estimates for the United Kingdom, which are roughly comparable with the German figures quoted above.

	(£000,000's)					
	1924	1925	1926	1927	1928	1929
National income	3,586		3,684	3,887	3,849	3,996
Home investment (after meeting depreciation)	218	459	240	215	214	168
Undistributed profits	167	162	128	186	168	169
Deduct losses and dividends (if any) of concerns making losses	— 9	— 17	— 19	— 20	— 14	— 16

² New capital issues are not a reliable guide even of the trend of investments. Cf., e.g., Clark, *op. cit.*, pages 136 and 137: "A scrutiny of prospectuses in recent years will show, however, that never more than 30 per cent of the new issues, and in some years less than 10 per cent, are in any sense 'net'. The bulk of all new issues goes for purchase of existing business and assets of all kinds".

as in the United Kingdom and the United States. There was no great inflow of borrowed money, and new investment took place mainly from domestic resources. Italy did not stabilise her currency till December 1927, and what import of capital took place after stabilisation was mainly a return flow of Italian capital which was invested in equities more readily than foreign loans might have been.

Indebtedness of Business Corporations as a Percentage of Owned Capital.
(Creditor countries.)

Year	Italy ¹			Netherlands ²		
	Capital	Debt	%	Capital	Debt	%
	Lire (000,000,000's)			Gulden (000,000's)		
1913	3.8	3.1	81.8			
1925	28.2	28.1	100.0	370	326	88.1
1926	33.3	32.8	98.6	376	328	87.2
1927	36.9	34.6	93.8	388	330	85.1
1928	40.0	35.9	89.7	418	339	81.1
1929	44.2	37.8	85.5	562	362	64.4
1930	47.6	39.6	83.2	536	369	63.0
1931	45.2	37.0	81.7	589	327	55.5

Year	United Kingdom ³			United States ⁴		
	Capital	Debt	%	Capital	Debt	%
	£ (000,000's)			\$ (000,000,000's)		
1913						
1925	2,730	1,600	58.6	93.7	...	...
1926	2,740	1,590	58.0	98.1	64.6	65.9
1927	2,850	1,610	56.5	107.3	67.3	62.7
1928	3,170	1,610	50.8	112.9	68.6	60.8
1929	3,100	1,560	50.3	121.6	73.5	60.4
1930	3,200	1,610	50.3	120.6	73.5	60.9
1931	3,200	1,600	50.0			

¹ Società Italiane per Azioni, *Notizie Statistiche*: The figures include all joint-stock companies, less financial and agricultural companies.

Owned Capital: Share capital and reserves.

Debt: Debentures and other creditors.

² Dr. A. Sternheim's figures, *Nederlandsche Konjunctuur Maart*, 1933, page 17. Eighty important companies.

³ Colin Clark: "The National Income", Appendix 1. Sample of balance-sheets of manufacturing and mining companies.

Owned Capital: All capital less debentures and creditors.

Debt: Debentures and creditors.

⁴ United States: Treasury Department, *Statistics of Income*, 1925-30. All joint-stock companies, less financial companies.

Owned capital: Share capital, reserves and balances carried forward.

Debt: Accounts and notes payable, bonds, mortgage and miscellaneous items not segregated by nature of liabilities.

In the capital-importing countries, the trend to increased indebtedness both absolutely and relatively to owned capital was unmistakable as soon as the capital adjustments after the inflation period had been carried through. Thus, in Hungary, the proportion of debt obligations to capital increased between 1927 and 1929 from 78.1 to 83.2 per cent. The increase in Germany between 1925-26 and 1929-30 was from 57.7 to 84.2 per cent. Roumania is a conspicuous exception to the general rule.

*Indebtedness of Business Corporations as a Percentage
of Owned Capital.¹*
(Debtor Countries.)

Year	Denmark			Germany			Hungary		
	Capital	Debt	%	Capital	Debt	%	Capital	Debt	%
	Kr. (000,000's)			RM. (000,000,000's)			Pengö (000,000's)		
1925 .	1,494	1,558	104.3	14.7	8.5	57.7	...		85.8
1926 .	1,567	1,278	81.6	16.6	10.8	65.1	...		69.3
1927 .	1,517	1,250	82.4				1,303	1,017	78.1
1928 .	1,476	1,185	80.3	18.7	15.3	81.8	1,404	1,225	87.3
1929 .	1,536	1,248	81.3	19.6	16.5	84.2	1,490	1,314	88.2
1930 .	1,759	1,465	83.3	19.3	15.8	81.9	1,542	1,238	80.3

Year	Poland			Roumania		
	Capital	Debt	%	Capital	Debt	%
	Zloty (000,000's)			Lei (000,000,000's)		
1925 .	...	...	...	25.2	30.0	119.1
1926 .	1,779	1,694	95.2	33.8	34.7	102.5
1927 .	2,561	2,088	81.5	41.2	39.1	95.0
1928 .	3,868	2,996	77.5	46.1	43.6	94.6
1929 .	4,600	3,769	81.9	50.6	46.6	92.1
1930 .				55.6	43.7	78.6

Such a development, which is not merely a post-war phenomenon but was characteristic also of pre-war periods of business expansion, raises difficult questions of international finance.²

¹ Denmark: *Statistisk Aarbog*, 1926-1932.

Germany: *Vierteljahrshefte zur Statistik*, 1926-1932.

Hungary: *Annuaire Statistique*, 1926-31 (industry only).

Poland: *Annuaire Statistique*, 1926-1930; *Informations Statistiques, Fascicule Spécial*, III, 1932; Polish companies only.

Roumania: *Buletinul Statistic al Romaniei*, 1932, No. 1, page 46.

In all countries, owned capital consists of share capital plus reserves, excluding special accounts such as staff pension funds.

² The proportion between borrowed and owned capital increased in Hungary from 57 per cent in 1905 to 78 per cent in 1907, fell after that year of crisis, but increased again from 68 per cent in 1910 to 79 per cent in 1912. In Prussia it rose from 76 per cent in 1905 to 85 per cent in 1907, but fell in 1908 to 79 per cent. In Germany as a whole it was 81 per cent in 1907-08, but fell to 67 per cent in 1908-09, rising again to 88 per cent in 1912-13.

The borrowing countries, because of the various factors that cause their shortage of capital, are not able to offer the security which is necessary to attract capital upon the ordinary risk-sharing basis. They tend, indeed, to find their capital for new investment largely from bank advances which are later repaid when the business, once established, is able to float a capital issue to be taken up by private investors. There is, therefore, a constant danger in periods of expanding trade that the investment promoted by means of bank advances based in part upon international borrowing will, in the downward turn of the cycle, prove embarrassing both to debtors and to creditors. It was largely this tendency to finance an over-expansion of business by means of debt, and especially foreign debt, which made many of these borrowing countries a source of weakness in the present depression.

There is a further important comment to be made concerning the indebtedness of industry as compared with the capital invested in the form of equities. As the preceding tables show, the absolute amount of indebtedness, even in the creditor countries, increased substantially in the case of the United States of America and remained approximately at the same level in the United Kingdom during the years 1925-1929. In the debtor countries, the increase of indebtedness was even more noticeable. Industry in general therefore carried a much heavier load of debt when the boom came to an end in 1929, and the fixed charges upon this debt remained as a depressing influence upon profits after earnings fell off in the depression. In such conditions as have persisted from 1929 to 1933, capital invested in the form of shares may be deprived of its dividends; but debt charges cannot be reduced except by agreement with the creditors or by default.

Moreover, there were peculiarly difficult aspects of this swollen indebtedness in the present depression. In the debtor countries, much of the borrowed capital had come to industry by foreign loans contracted through the banking systems, and the inability of industrial enterprises to meet their obligations therefore shook the stability of the banks which had borrowed in order to promote industrial investment. There was not only a transfer problem involving foreign exchange difficulties, but the liquidity of the banking systems was imperilled.

In many countries, too, there was a marked tendency for industrial borrowing to take the form of long-dated bonds or debentures that could not easily be converted into less onerous debts as interest rates fell. Thus, in the United Kingdom, the issues of debentures rose from 58 per cent of all borrowed capital in 1924 to 68 per cent in 1929.¹ In the United States of America,

¹ Clark, *op. cit.*, page 143.

bond and mortgage indebtedness rose from 25 per cent of the total business indebtedness in 1926 to 50 per cent in 1929.¹

Apart from the tendency for indebtedness to grow relatively to actual share capital, there was a more universal tendency towards a change in the nature of the share capital itself. Partly because of the increase in the number of small shareholders, and in the amounts of capital accumulated by financial institutions such as insurance companies as the result of widely dispersed small savings, but partly also because of the more general insecurity of business enterprises in such a disturbed period, there was a strong incentive to seek investment in preferred rather than in ordinary shares carrying the full risks of industry. In the United Kingdom, for example, there was, between 1924 and 1929, an increase in the proportion of preferred shares,² and the same tendency may be seen in the United States of America.³

The effort made by large corporate enterprises to maintain regular dividends was partly in response to this tendency for investors to seek the greater security of preferred shares or debentures. The importance of offering a greater measure of security strongly reinforced the trend of professional management towards policies of maintaining regular, equalised dividends. Further reference will be made to this aspect of financial policy in the later section dealing with the depression period.⁴

Another element of rigidity to which special reference is necessary was the influence exerted, not only upon the burden of indebtedness, but also upon the dividend policies of corporate enterprises, by the high interest rates upon industrial investments, particularly on long-term, that ruled after the war.⁵ These high interest rates were maintained by a combination of causes, among which may be mentioned the existence of a large amount of war loan issued at high rates, the actual shortage of capital in many countries in the post-war period and the great degree of political and economic insecurity that prevailed. It is true that, for some months during the boom period, exceptionally low rates of short-term interest were prevalent on the chief financial markets. These did not, however, bring about a lowering of the long-term rates and the possibilities of financing

¹ *Statistics of Income*, published by the United States Treasury.

² In the case of the companies included in the *Economist's* statistics, the preferred capital was, in 1924, 56.5 per cent of the common stock and, in 1929, 58.4 per cent.

³ According to *Statistics of Income*, published by the United States Treasury, preferred stock represented, in 1924, 22.7 per cent of common stock, in 1926, 27.4 per cent and, in 1929, 24.1 per cent.

⁴ See below, pages 145-6.

⁵ Keynes, "The Future of the Rate of Interest", Index Vol. V, No. 57, September 1930.

industrial enterprises in the short-term market are limited. It is obvious that the continuance of high interest levels not only made the increased indebtedness of industry a much heavier burden upon its earning capacity, but also created the necessity for maintaining dividends at levels sufficiently high to compete with the opportunities for investment offered by bonds whose yield was influenced by the existence of war loans with a high fixed interest.

In the preceding discussion, attention has been focussed upon the actual capital structure of corporate business enterprises as stated in their balance-sheets. Tentative though the analysis must be in the absence of more complete and authoritative data, it is all in the direction of suggesting that the course of real investment in most countries before 1929 was such as to overrun the actual savings of the community. No account has been taken up till now of the fact that, particularly in the later stages of the boom before 1929, there was a considerable rise of capital values in the security markets. Some of this rise, which was the result of one of the most sustained speculative markets ever known, was transferred to the actual valuation of industrial capital. In the course of the boom, there were numerous examples, not only of new capital flotations, but also of consolidations, mergers, the formation of holding companies and similar expedients by which the capital of existing enterprises was transformed into new and watered capital valuations of old and new enterprises. Moreover, the rise of security values was intimately associated, in the United States of America at least, with the financing of new issues by means of bank advances upon industrial securities as collateral. When the Stock Exchange boom broke, the rapid decline of security values reduced them to levels much more closely approximating the actual capital valuation of the enterprises and therefore, presumably, to their earning capacity. But that part of the increased speculative values which had been consolidated by recapitalisation operations of various kinds, as well as many of the new enterprises floated in the speculative period, remained. When the depression began, therefore, the capital structure of many countries carried this triple burden of investment beyond their real savings, including many unsound new enterprises floated during the boom, of greatly increased debt charges and of watered capital in many re-organised enterprises. Interest rates remained high, and, in addition, there had developed a strong tendency towards the maintenance of equalised dividends. The combination of all these factors strained industrial earnings and severe liquidation was inevitable. The prospect of such liquidation was bound to impose a severe strain also upon the banking systems of many countries.

THE EFFECTS OF THE DEPRESSION UPON BUSINESS EARNINGS.

There is always a lag between business earnings and their distribution as dividends. In the final stages of expansion, earnings are high, but the dividends reflecting them may not be declared until after depression has set in. When the break comes and industrial prices and output decline, the management of corporate enterprises is directed towards cutting costs and particularly prime costs such as wages. Wage-rates are not immediately or easily reduced under present conditions, but unemployment quickly increases and therefore a part of the burden of the depression falls immediately upon the wage-earners and upon the Governments which contribute to their support. But there is a strong probability that the business profits earned in the previous period of expansion will be distributed even after the depression has set in.¹

This probability is reinforced by the policy pursued by many conservative and sound enterprises which have built up large reserves in the good years with the definite object of maintaining steady dividend policies in the interests of the small investors. Even in a prolonged depression, reserves may be available for maintaining dividends, and only with reluctance are dividends reduced. In the long run, however, such a serious depression as that which has persisted from 1929 till the present time forces all but the strongest concerns, not only to a reduction of dividends, but to an adjustment of their debts and, in some cases, to a writing-down of share capital.

The dearth of statistical material naturally becomes greater as one attempts to study the most recent period and only fragmentary evidence can be adduced in support of the tentative conclusions stated below. There can be no doubt, however, that business earnings have decreased almost catastrophically in most countries. Thus the net earnings of all business enterprises in Belgium are estimated to have fallen from 4,384 million francs for accounts closed in 1930 to 582 millions in 1932. In Germany, industrial earnings, expressed as a percentage of owned capital, fell rapidly from their peak of 7.2 per cent in 1927 to a loss of 4.8 per cent in 1931. In the United States of America, the net earnings of business corporate enterprises fell from 7,551 million dollars in 1929 to a loss of 1,524 millions in 1931.

These examples may be supplemented by a summary table

¹ Cf., e.g., the diagram showing such a development reproduced in the *International Labour Review*, March 1933, page 395.

showing for several countries the net earnings of business corporations in the years 1929 to 1932 as a percentage of the base year 1928. Wherever possible, a distinction is made between the earnings of financial and industrial enterprises.

*Net Earnings of Corporate Enterprises in Certain Countries,
1928-1932.*

(Base 1928 = 100.)

(Indices based on actual net earnings in national currencies.)

Country	Type of Corporation	1929	1930	1931	1932
Argentine † :	Business	98	81	61	...
	Financial	103	96	85	...
	Total	99	83	64	41*
Belgium † :	Business	116	118	71	16
	Financial	123	161	142	68
	Total	118	128	88	29
Denmark † :	Business	104	95	...	...
	Total (incl. Financial)	183	165	...	...
Germany †† :	Business	84	57	— 66	...
	Financial	92	65	—295	...
	Total	86	59	—112	...
Hungary † :	Industry (a)	104	86	62	...
	Total (excluding Financial) (a)	103	84	61	...
Italy † :	Industry † (b) . . . . .	...	...	40	— 7
	Business	111	— 4	7*	...
Netherlands †† :	Business	112	29	4	...
	Financial	103	57	53*	...
	Total	109	7	17*	...
Roumania † :	Industry	104	91	76	...
United Kingdom †† :	Total (a)	103	85*	68*	65*
	Manufacturing and Mining (b)	108	90	72	...
	Transport, Distribu- tion (b)	104	95	75	...
	Overseas (b)	94	66	...	...
	Business (a)	111	15	— 22*	...
United States † :	Financial (a)	85	— 36	—103*	...
	Total (a)	106	19	— 36*	...
	Business (b)	118	67	26	—0.3

For sources see following page. — * Provisional.

† All companies included in national statistics.

†† Index calculated by chain method for representative sample of corporations.

† It is assumed that the net earnings in 1930 were 86 per cent of those in 1928, when calculated by chain method for representative sample of corporations.

For several of these countries, more detailed information is available showing the movement of profits in the main groups of enterprises. These statistics for the most part refer to fairly representative samples, rather than to complete information covering all corporations. They are sufficient, however, to show that the depression has hit industry, trade and finance rather unevenly both in time and in degree. There are such different factors operating in particular industries in the various countries that no general summary is possible ; but it is not difficult to pick out instances of sheltered groups and of groups which have suffered with exceptional severity. Thus, in the United Kingdom, the relative prosperity of the electrical and motor-car industries, and of certain industries which are largely sustained by the domestic market, is in striking contrast with shipping, ship-building and certain exporting industries. In Germany, there is a much larger number of industrial groups which have suffered heavily, but domestic commerce, insurance, public utilities and the lignite industry have survived fairly well, while on the contrary there are heavy losses in shipping, banking, transport, construction and such exporting industries as the electro-chemical group.

Sources of data for individual countries in the table on preceding page.

- Argentina : Banco de la Nacion Argentina, *Economic Review*, October 1932, page 91 ; *Revista Economica*, December 1932, page 207.
Belgium : Banque nationale de la Belgique. *Bulletin d'Information et de Documentation*, April 1929 (special number), March 25th, 1930 and 1931, April 25th, 1932 and 1933.
Denmark : *Statistisk Aarvog*, 1931-32. *Statistiske Efterretninger*, 1933.
Germany : *Wirtschaft und Statistik*, second August Heft, 1930-32.
Hungary : (a) *Annuaire de Statistique de la Hongrie*, 1931-32. (b) Ungarisches Institut für Wirtschaftsforschung, December 1932, March 1933.
Italy : Societa Italiana per Azioni, *Notizie Statistiche*.
Roumania : *Buletinul Statistic*, 1931-32 ; *Anuarul Statistic*, 1931-32.
Netherlands : *De Nederlandsche Conjunctuur*, March 1932, page 16, December 1932, page 30.
United Kingdom : (a) *Journal of the Royal Statistical Society*, Part IV, 1932 ; Stamp, "Industrial Profits" ; Bank of England, Statistical Summary, July 1933. (b) *Economist*, April 30th, May 7th, 1932.
United States : (a) Treasury Department, *Statistics of Income*, 1928-1930 ; Preliminary Report, 1931. (b) Federal Reserve Bank of New York, *Monthly Review*, April 1932, 1933.

The figures for Argentina, Belgium, Denmark, Hungary, Italy, Roumania and the New York Federal Reserve Bank's estimates of company earnings are credited to the year in which the accounts were closed, and therefore lag somewhat behind the period during which the profits were actually earned.

The figures for Germany refer to accounts closed in the last quarter of each year, approximately 70 per cent of total earnings, and therefore reflect with fair accuracy the earnings of that year. For the United Kingdom, the estimates are based upon company reports so chosen that their earnings reflect total earnings in that year.

The United States Treasury Statistics refer to the year in which profits were actually earned. The Federal Reserve Bank's estimates therefore should be compared rather with the preceding year's Treasury estimates than with the current year.

In the United States of America, certain industries based primarily upon the expanded prosperity of the boom period — the automobile, film and household equipment groups — together with their suppliers, particularly the steel industry, have suffered heavily.

The statistics quoted in the preceding paragraphs refer to the earnings of already established companies. It is clear that such earnings fell off greatly in the years 1931 and 1932 and that the maintenance of dividend payments upon existing share capital was rendered possible only by drawing upon accumulated reserves. In some countries and in some industries, in most countries, the strain imposed upon such reserves by reduced earnings or actual losses had, by 1932, become so great that reduction of dividends and the writing-off of lost capital was forced in an increasing number of instances.

Since it is probable, as Sir Josiah Stamp has shown,¹ that profits are more closely correlated with production than with any other factor, the almost universal shrinkage of production during 1932 points to a reduction of earnings which will probably be reflected in the statistics of profits that will be declared early in 1933. The possibility of earning a profit upon the nominal capital of existing enterprises depends partly upon the extent to which that nominal capital was adjusted after the previous depression of 1920-21, and also upon the extent to which it was swollen in the years of expansion from 1925-1929. Where reconstruction and writing-down was effective after 1921 and conservative policies were followed in regard to capitalisation and reserves during the boom, the ability to pay dividends during the depression is obviously greater. Where, on the other hand, there was inadequate reconstruction after 1921, or where liberal stock dividends were distributed and inadequate reserves were set aside during the boom, present earnings are far more out of proportion to the nominal capital invested.

The extent to which the decline in the earnings of already invested capital affects the opportunities for profitable new investment is discussed later. Before approaching this subject it is necessary to draw attention to the importance of the dividend policies pursued by existing enterprises.

The payment of dividends, and still more of debt service, has been maintained much more successfully than the statistics of corporate earnings might suggest. This was particularly the case in the first two years of the depression. In the United Kingdom, for example, the dividend distributions in 1930 were greater than, and in 1931 and 1932 approximately as great as, in 1929, when the

¹ *Journal of the Royal Statistical Society*, Vol. XCV, Part IV, 1932.

figures were well above the average of preceding years. In order to achieve this result, however, the proportion of profits placed to reserve fell heavily from 22.3 per cent in 1928 to 7.4 per cent in 1932. There has been the same tendency to maintain dividends by diminishing the amounts set aside as reserves, and by drawing upon previous reserves, in almost every country. This, of course, is one of the objects for which reserves are accumulated in good years, and the policy of large corporations in thus equalising the returns from investment in good years and bad is an important stabilising influence — maintaining purchasing power and encouraging the small investor by offering him greater security for his savings. As the depression persists, however, and the earnings of business enterprises continue to fall while their reserves are depleted, there comes a time when the policy of maintaining dividends becomes impossible in many industries. This is particularly true when industry is heavily loaded with debt obligations.

In the table which follows, statistics are given for a number of countries showing the decline in earnings and the extent to which dividends were maintained in the depression years. It will be seen that there was a tendency for dividends to consume an increasing proportion of business earnings, but the fall in earnings was such that the actual amounts paid as dividends decreased in 1932, and in some countries earlier.

It is clear that, in the later years of the depression, the maintenance of dividends at their former levels has proved impossible for the majority of businesses in most countries. In the first stages of the depression, there was a general feeling that purchasing power should be maintained. Attention was drawn in the *Survey* for 1931-32 to the attempts made to defend wage-rates, debt service and public expenditure.¹ The maintenance of dividends fitted into such a policy and was defended, apart altogether from the financial position of the companies immediately concerned, as a necessary measure to maintain purchasing power and consumption. The regular payment of dividends also contributed to the maintenance of Stock Exchange values for a time.² By the end of 1932, however, it was abundantly clear that purchasing power was not being, and could not be, maintained. Drastic readjustments of incomes were inevitable and, among those readjustments, the reduction of dividends had an important place.

¹ Pages 230 to 232.

² A Dutch economist, J. Tindbergen, after investigating a number of Dutch companies over a series of years, concludes that the last dividend paid was the dominating factor in determining share values. Cf. *De Nederlandsche Conjunctuur*, December 1933, page 16.

*Business Earnings and Dividends in Certain Countries, 1928-1932.*¹

	1928	1929	1930	1931	1932
Belgium :					
1. Net earnings of corporations showing net income (francs 000,000's)	5,264	6,159	7,043	5,543	3,457
2. Dividend of all corporations as a percentage of 1	55	56	57	64	71
Denmark :					
1. Net earnings of corporations, showing net income (Kr. 000,000's)	157	171	172	...	...
2. Dividend of the same corporations as a percentage of 1	76	77	74	...	...
Germany :					
1. Net earnings of corporations, showing net income (RM. 000,000's) .	1,516	1,460	1,053	...	...
2. Dividend of all corporations as a percentage of 1	81	86	87	...	...
Italy :					
1. Net earnings of corporations, showing net income (Lire 000,000's)	3,203	3,445	2,985	(2,221)	...
2. Dividend of all corporations as a percentage of 1	78	80	80	(78)	...
United Kingdom :					
1. Net earnings of manufacturing and mining corporations, showing net income (1924 = 100)	104	113	100	.	.
2. Dividend of the same corporations as a percentage of 1	75	76	79	.	.
3. Net earnings of transport and distribution corporations, showing net income (1924 = 100)	115	120	111	.	.
4. Dividend of the same corporations as a percentage of 3	83	84	86	.	.
United States :					
1. Net earnings of corporations, showing net income (\$000,000's)	10,500	11,543	6,321	...	...
2. Dividend of the same corporations as a percentage of 1	63	68	108	...	...

¹ Belgium, Banque Nationale, *Bulletin d'Information*; Denmark, *Statistisk Aarboeg*; Germany, *Statistisches Jahrbuch, Wirtschaft und Statistik*, the figures refer to the period from July 1st to June 30th of the following year; Italy, Società Italiane per Azione, *Notizie Statistiche*; United Kingdom, *Economist*, April 30th, May 7th, 1932; United States, *Statistics of Income, 1928-1930*.

The figures for the United Kingdom and the United States refer to the year of income; for all other countries to the year in which the accounts were closed.

Opportunities for profitable new investment as interest rates and prices fall have, in past depressions, been an important factor in forcing capital reconstruction of existing industries. The greater part of new investment, it is true, proceeds by extension of already established enterprises. In so far as these have strained their earning capacity and depleted their reserves in an effort to maintain dividends upon their share capital, they have been unable to proceed with programmes of re-equipment or to free themselves from their heavy debt charges. In previous depressions, new enterprises have tended to force their established competitors to just such processes of reconstruction, even at the cost of reducing or foregoing dividends or of re-constituting their share capital.

The failure of such new enterprises to emerge up till the present appears to be due to a variety of factors partly connected with the price of investment goods relative to the price of finished consumption goods, but partly due also to general insecurity. For the reasons set out in previous chapters,¹ the discrepancy between the prices of production and consumption goods has constantly tended to widen, so that costs of production have remained high and investment has not been profitable. Moreover, though credit has been abundant and short-term interest rates have fallen to exceptionally low levels, the rates of interest charged upon industrial loans have not fallen greatly. In many countries, the banks have been afraid to endanger their liquidity by extending industrial loans² which are not self-liquidating within a short period. In addition, there has persisted a heavy risk premium in consequence of the continued extension of Government interference with industry and trade in an effort to protect existing industries from new or aggravated competition. There has been little incentive to new investment in a world which has multiplied tariffs, quotas, exchange controls and other forms of interference with private initiative.

The failure of new competing enterprises to emerge and force a readjustment of existing businesses is therefore partly due to the pressure upon public authorities from those who are reluctant to face such a readjustment and are able to secure public support to a degree never known in any previous depression. The reluctance to face drastic revaluations of invested capital has been in part due to the combination of factors to which attention was drawn in the preceding sections of this chapter.

¹ See Chapters II and III. Cf. also *Vierteljahrshefte zur Konjunkturforschung*, 1933, page 210.

² Cf. National Industrial Conference Board, "The Availability of Bank Credit", New York, 1932, *passim*, and *Vierteljahrshefte zur Konjunkturforschung*, 1933, page 191.

The greater volume of indebtedness, especially that part of it which was borrowed in foreign countries and came to industry through bank advances, the increased use of debentures and preference shares and the general demand of small investors and financial institutions for continuity of dividends are very important factors in the situation. The plight of the financial institutions and banking systems in many countries, to which attention is drawn in a later chapter, is a further powerful influence in the direction of conserving the existing capital structure.

In addition, however, there must be reckoned the widespread disposition to shrink from the catastrophic solution of the crisis by means of bankruptcy and to invoke the aid of the banking systems and, in certain cases, of the public credit in staving off the hardships which would be involved therein. There has been a disposition to seek a solution along other lines, by monetary action designed to raise the price-level, by protective governmental intervention, or by organisation to restrict and regulate production and trade.

Such solutions had not been found in effective measure by the end of 1932 and, in many countries, the continued aggravation of the crisis had led to a situation in which financial and currency difficulties were beginning to force both a diminution of dividends and capital revaluation. The banking crisis in the United States in February 1933 was the most important example. Large numbers of banks which had strained their credit in extending loans to their customers upon the basis of real estate and industrial security values that proved exaggerated found themselves unable to withstand the panic that set in when their depositors lost confidence. Temporary measures, such as the activities of the Reconstruction Finance Corporation, which might have proved adequate to tide, not only the banks, but some of their customers, over an ordinary depression, were inadequate to save the situation that had, in fact, developed as a result of widespread speculation. Capital reconstruction, both of the banks and of industry in general, proved necessary in many cases.

This example, however important in itself and significant also because of its far-reaching effects, by no means exhausts the consequences that followed from the extreme difficulty of maintaining intact the capital structure that had been built up in the course of the boom. The burden of ownership claims upon the product of industry contributed its large share to the combination of forces that has driven many countries to abandon or restrict the working of the gold standard. A particularly difficult situation has been created where industrial expansion was largely based upon foreign capital and where the inability of

industry to carry the charges thus imposed upon it has resulted in a paralysis, not only of domestic production, but of international financial transactions. The manner in which the effort to discharge foreign debt obligations and, at the same time, maintain currency stability has led to the increased trade restrictions which are throttling international commerce is treated elsewhere, but its obvious connection with the over-capitalisation of industry is relevant here. A further important consequence of the maintenance of existing capitalisation has been the difficulty of reducing the unit-price of goods produced in manufacturing industry and of thereby reducing the discrepancy between the prices of finished goods and raw materials, which is an outstanding obstacle to recovery from the depression. From many points of view, therefore, the disproportion of the claims of ownership to the earning capacity of industry proved a serious obstacle to recovery.

THE PLIGHT OF AGRICULTURE.

The circumstances under which farming is conducted differ so widely from country to country, and, in particular, between the Old World and the New, that international comparisons are difficult. There is a sense in which farmers in all countries are more fortunately situated than urban workers, because they normally may be sure of at least the elementary necessities of life. But, in the so-called "peasant countries", this advantage is more obvious than in those where agriculture is highly commercialised and where the farmer conducts a "farm-factory" producing a narrow range of specialised products, relying on his cash income to purchase even food in many cases.

There is a preliminary distinction to be drawn between the countries where the exportation of an agricultural surplus is an important, if not the principal, source of purchasing power in the world's markets, and those countries where agricultural production is essentially for the home market. In the latter case, agriculture is almost always sheltered by protective tariffs, which in recent years have been supplemented by prohibitions, quota systems and other quantitative import restrictions in quite exceptional degree. The following table is perhaps sufficient to illustrate the fact that, in the countries where agriculture is primarily for the home market, the fall in agricultural income has been notably less severe than in the countries where the export market is of dominating importance. It will be clear, also, that the fall in agricultural income in the countries exporting mainly commodities for direct human consumption came later than in that of the countries exporting mainly industrial raw materials.

Gross Value of Farm Production,¹
National currency (000,000's.)

Season	France	Germany	United Kingdom	Switzerland
	Francs	RM.	£	Francs
1924 or 1924-25 . .	2	11,100	2	2
1925 or 1925-26 . .	.	11,631	300	.
1926 or 1926-27 . .	.	12,085	288	.
1927 or 1927-28 . .	.	12,879	292	1,395
1928 or 1928-29 . .	.	13,865	293	1,467
1929 or 1929-30 . .	74,990	13,340	294	1,479
1930 or 1930-31 . .	61,770	11,654	273	1,371
1931 or 1931-32 . .	.	9,889	263	1,403
1932 or 1932-33 . .	.	8,800	...	1,281 *

Season	Argentine	Australia	Canada	United States
	\$ oro	£ A	\$ C	\$
1924 or 1924-25 . .	2 4	279	2	2
1925 or 1925-26 . .	1,011	251	1,709	11,300
1926 or 1926-27 . .	868	257	1,715	12,000
1927 or 1927-28 . .	792	259	1,826	11,500
1928 or 1928-29 . .	1,009	257	1,806	11,600
1929 or 1929-30 . .	1,055	211	1,631	11,700
1930 or 1930-31 . .	954	183	1,268	11,900
1931 or 1931-32 . .	614	177 *	815	9,400
1932 or 1932-33 . .	641	...	712	7,000
1932 or 1932-33 . .	567	...	...	5,200

Season	Denmark	Irish Free State	New Zealand	Greece
	Kr.	£	£ N.Z.	Drachmæ
1924 or 1924-25 . .	2 3	2 3	2	2
1925 or 1925-26 . .	1,499	43	77	.
1926 or 1926-27 . .	1,344	38	68	.
1927 or 1927-28 . .	1,038	37	67	.
1928 or 1928-29 . .	1,087	39	77	.
1929 or 1929-30 . .	1,141	40	82	11,268
1930 or 1930-31 . .	1,195	40	72	8,462
1931 or 1931-32 . .	1,133	38	57	7,776
1932 or 1932-33 . .	951	33	50	7,494
1932 or 1932-33 . .	816	...	...	9,393

* Provisional.

¹ Sources: France: *Supplément au Bulletin Quotidien*, July 27th, 1932.
There are preliminary indications of an increase for 1931-32.
(For continuation of footnotes, see following page.)

In the first group, where agricultural exports are less important, the fall in agricultural income was of a much lower order of magnitude than in the agricultural exporting communities. Even allowing for differences in methods of calculation, these disparities are certainly significant.

It should be remembered also that, for all of the exporting countries included above, with the exception of the United States, currency depreciation had taken place before the end of 1932. Thus, in New Zealand, the total value of agricultural production, which was at its peak in 1928 at £82 million, fell in 1931 to £50 million; but the New Zealand £ had also fallen 10 per cent below sterling, or to about two-thirds of its gold parity, so that the value of New Zealand production measured in sterling should be reduced by about 10 per cent.

Broadly speaking, the agricultural communities in dominantly industrial lands have been sheltered by governmental protection and have suffered less from the depression than either their competitors in the agricultural exporting countries or most other economic groups in their own lands.⁵

Those European countries in which agriculture is largely an export industry have been affected with extreme severity in the depression. The Danubian wheat-producing countries may be taken as illustrative. Their situation is universally recognised as presenting one of the most difficult aspects of the agricultural

Germany: Institut für Konjunkturforschung: *Wochenbericht* V, No. 51. *Konjunktur-Statistisches Handbuch*, 1933.

United Kingdom: Clark, "The National Income", page 110. "The Agricultural Output and the Food Supplies of Great Britain."

Switzerland: *La Vie économique*, January 1929-1932, February 1933. Preliminary estimates in previous years have proved to be too low.

Argentina: *Revista Económica Argentina*, January-June 1929, page 88, September 1932, pages 155, 159. For 1927, the gross value of agricultural production was estimated to be \$ m/n 3,570,000,000, and in the same year the exports, of which 95 per cent are agricultural products, amounted to \$ m/n 2,294,000,000.

Australia: *Quarterly Summary of Australian Statistics*, March 1933.

Canada: *Monthly Bulletin of Agricultural Statistics*, March 1933. *Canada Year-Book*, 1931, 1932.

United States: *Agricultural Year-Book*, 1932, Bradstreet.

Denmark: *Statistiske Efterretninger*, January 1925-1933. "Value added" by agriculture amounted in 1924-1926 to Kr. 1,288 million and in 1929 to Kr. 1,128 million, *Nationaløkonomisk Tidsskrift*, 1932, page 130.

Irish Free State: *Statistical Abstracts*, 1931, 1932; 44 per cent of the total agricultural output was exported in 1926-1927, and 49 per cent in 1929-1930.

New Zealand: *Monthly Abstract of Statistics*, January 1933.

Greece: Bank of Greece, "The Economic Situation in Greece", 1932.

¹ Calendar year.

² Exports of agricultural products.

³ All exports.

⁵ Farmers' income in Germany dropped 18.6 per cent from 1929 to 1931, while the national income dropped by 25 per cent (*Statistisches Jahrbuch*, 1932, page 526). In the United Kingdom, the national income is estimated to have been reduced by 12.4 per cent from 1929 to 1931, while farmers' gross income was reduced by 10.5 per cent (Clark: "The National Income 1924-1931", pages 70 and 110).

crisis. The heavy fall in the price of cereals, and especially of wheat, together with the closing of their former markets, has gravely reduced farming incomes and driven the peasantry back towards subsistence agriculture. In Roumania, agricultural exports were valued at 172.5 million dollars in 1929 and only 99.1 in 1932, while in Hungary the comparable figures were 181.8 in 1929 and 58 in 1932.¹ The other agricultural countries of Central and Eastern Europe, outside of the wheat belt, have been very seriously affected also. In Greece for example, where agricultural exports average 90 per cent of the total, the value of that total fell from 90.3 million dollars in 1929 to 34.8 million in 1932.

The plight of agriculture in these European lands is paralleled by the difficulties into which farming has fallen in the producing areas outside of Europe — in North and South America, Australia and New Zealand, and parts of Asia and Africa. There is, however, a distinction to be drawn between the situation in those countries where farming is highly mechanised and organised financially upon modern lines, and those where the export surplus consists characteristically of peasant production. In the United States, the Argentine and the British Dominions, farming is a business, in many respects the most important business, of the whole community. The same is true of many tropical areas, such as the Dutch East Indies² and Hawaii, where the large-scale plantation system has been developed, or where peasant production has been highly organised for the export market, generally under European or American supervision. The collecting for export of the surplus peasant production in such countries as India and China tends to be less highly organised financially, and a drastic fall of prices, while serious enough, does not normally derange the whole financial structure of the country in quite the same degree. The peasant can usually live upon his holding and, while the diminution of his export receipts impoverishes both him and the commercial structure built upon his prosperity, it does not loom as large in the whole national economy as the similar fall in prices has loomed in countries such as Australia, the Argentine and the United States. It is, however, essential to remember that the depression has brought great difficulty, not only to the dairy farmers of countries like Denmark, to the wheat-growers in the Danubian basin and to the farmers of America and the British Dominions, but also

¹ League of Nations, *Monthly Bulletin of Statistics*.

² The total dividends paid by the plantations in the Dutch East Indies to shareholders abroad was, in 1928, 171,000,000 florins; in 1930, 97,000,000; and, in 1931, 17,000,000 florins. *Korte Berichten voor Landbouw, Nijverheid en Handel*, June 17th, 1932, page 620.

to vast multitudes of small farmers, particularly in Asia, who are only dimly aware of the world forces at work. The extent of their difficulty is indicated by the amount of gold which has been given up by the Indian people under the combined effect of a higher monetary price for gold and economic stress.

The strain upon the peasants in heavily populated and poor countries is naturally reflected in the social and political unrest which has been so widespread in recent years. Brought within the network of world trade by initiative from without, the peasants who are impoverished by its breakdown can hardly be expected to understand or be patient under the strain. It is not without significance that years of economic depression should be years of political and social difficulties.

Farmers in the progressive agricultural communities of North and South America, Australia and New Zealand have been hit by the full blast of the depression. The three outstanding reasons for the aggravated nature of their difficulties are that they are organised upon the expectation of continuing development, that borrowed capital plays such a large part in their finances, and that the export market is of overwhelming importance, not only in the determination of their prices, but in the whole national economy. Some of these difficulties they share with farmers in other lands ; but the combination is largely confined to the areas mentioned.

The capitalist organisation of farming in these newer lands is of a type which is quite foreign to Europe. Less rooted to the soil, and with far less regard for tradition, the farmer tends to regard himself less as the custodian of a heritage to be conserved, and more as a business man exploiting to the full the possibilities of the market. Conservation is of less, and speculation of more, importance in his outlook. He will use new methods, mechanical improvements in cultivation, co-operative experiments in marketing and the like, and will avail himself freely of the unusual facilities offered in such countries for borrowing both upon long and upon short term at reasonable interest rates. The whole recent background of farming in these lands, unlike that of Europe, has been one of expansion. Past periods of falling prices and depression are forgotten in the fact that even during such setbacks the frontier was pushed further out, new land brought into cultivation, and the foundations laid for further prosperity. Rising land values, which the farmer-owner in most cases expects to capitalise by selling his holding, have been the embodiment of such prosperity, and the whole financial structure of farming has tended to anticipate and discount such appreciation. The end of a boom period invariably finds the future discounted so heavily that the land is burdened with indebtedness

which would be heavy even if prices and land values were to be stabilised at boom levels, and is quite impossible when such levels give way to more sober valuations. Thus, a recent calculation of the debt situation in the United States estimates the farm mortgage indebtedness as \$4,900 million in 1913, \$8,232 million in 1921 and \$9,500 million in 1929. The peak was reached in 1925, when prices of agricultural produce were at their highest point in the post-war period.¹

*Agricultural Indebtedness in the United States.*²

	1913	1929	1930	1931	1932
1. Current value of agricultural capital (\$000,000,000's)	47.8	58.1	52.7		
2. Mortgage debt (\$000,000,000's)	4.9	9.5	9.2	9.4	.
3. Agricultural gross income (\$000,000,000's)	7.0	11.9	9.4	7.0	5.2
4. Interest on mortgage as a percentage of 3 (per cent)	3.4	4.7	5.8	7.7	10.0
5. All interest expenditures as a percentage of 3 (per cent)	—	5.5	7.0	9.5	12.9

There is a striking similarity of development in the farming situation in all of these newer countries, and land values, depending largely as they do upon export prices in world markets, follow much the same course in all of them.³

The natural corollary of "farming for the property rather than the produce market" is a very large use of borrowed capital. The extent of farm indebtedness, either on short or on long term, is not easy to calculate with precision; but its burden is obviously greater when the prices of agricultural produce have fallen 55 to 60 per cent from the 1929 levels. The average farm family in the United States had a cash income during 1924-1929 of approximately \$600 per annum; but, in 1932, this cash income had fallen below \$100. These estimates are for the cash income

¹ Subsequent land speculation in the years 1925-1929 was directed mainly to urban real estate, the indebtedness upon which is estimated to have risen from \$15,120 million in 1921 to \$33,125 million in 1929. Cf. Lionel D. Edie in *The Iron Age*, January 5th, 1933, page 26.

² Cf. *Agricultural Year-Book*, 1932, pages 892, 893 and 912; *Bradstreet's Weekly*, 1933; Lionel Edie: "New Year opens in Midst of Major Debt Adjustments", *Iron Age*, January 5th, 1933.

The estimated figures for 1931 and 1932 are based on the assumption that interest expenditures in these two years were the same as in 1930.

³ Cf., e.g., the diagram illustrating the similarity of the course of land values in New Zealand and the United States of America, between 1914 and 1924. *Economic Record*, May 1927, page 51(a).

remaining after interest and taxes were paid ; but, in view of the great reduction in cash receipts, it is easy to understand why, in a great number of cases, interest and taxes have not, in fact, been paid " because of pressing needs for more than \$100 of cash for other purposes. ¹

Land values have shrunk considerably, but not, as yet, in proportion to the fall in income. The mortgage debt, and still more short-term debt, has increased in the depression. The average value of the owner's equity, which, in the United States, had been \$8,191 in 1920, fell by 1930 to \$5,436, and has since fallen much more heavily. In face of these facts, it is not difficult to understand both the resistance to forced sales and tax distraints which has spread widely in certain States and the serious consequences of the farmers' difficulties upon other parts of the economic structure, notably the banks and the financial institutions which hold mortgages upon rural property.

Accurate up-to-date information concerning the indebtedness of most of the other overseas exporting countries is not available; but preliminary investigations in Canada suggest that farm indebtedness there may be heavier than in the United States of America, and has not decreased in the depression years.²

In most of the overseas countries, there was some relief from the rise in sterling prices for a few months after they had followed the lead of the United Kingdom in abandoning the gold standard. In most of them, also, the heavy burden of external indebtedness, expressed in terms of sterling, was mitigated, or at least prevented from becoming heavier, when they were thus cut off from the continuing fall in gold prices. In the case of Australia and New Zealand, as well as in that of Japan, currency depreciation went further than the fall of sterling, and so gave some temporary relief to the farming community, whose prices rose in terms of the local currency, while their costs for a time remained stable or were even reduced. Such relief, however, could only be temporary, and was promptly offset by similar currency depreciation in competing countries.

For certain European countries, sample investigations of farm incomes and expenses are available for 1928-29 in a volume containing the results of national studies collected and published by the International Institute of Agriculture at Rome. ³ From that volume the following summary table has been compiled.

¹ Cf. John D. Black, " The Agricultural Situation ", *Harvard Business Review*, January 1933.

² Cf. Report of the Minister of Agriculture for the Year ended March 1932. Ottawa, 1932.

³ " Farm Accountancy : Statistics for 1928-1929 ", Rome 1932.

Farm Income, Expenses and Debt 1928-29.

Country	Number of farms investigated	Gross income per hectare (Swiss francs)	Gross expenses per hectare (Swiss francs)	Labour ¹	Depre- ciation ²	In- terest ³	Debt ⁴ as per- centage of farm capital
				As a percentage of total expenses			
				Per cent	Per cent	Per cent	
Peasant farms :							
Austria	743	318	352	46.5	5.5	23.4	5.4
Czechoslovakia	228						13.8
Denmark	599	1,116	1,069	31.8	0.2	14.6	...
Estonia	260	166	187	50.6	7.7	18.4	15.9
Finland	474	348	413	42.3	4.4	25.7	14.1
Latvia	132	147	185	47.1	10.3	15.6	9.5
Lithuania	95	160	206	40.3	9.9	30.8	5.6
Netherlands	2,201	1,072	950	26.3	—	34.3	...
Norway	172	944	1,115	35.2	—	24.9	...
Poland	855	340	389	34.1	11.6	34.8	7.3
Sweden	242	500	567	46.7	—	20.6	...
Switzerland	504	1,259	1,421	39.7	10.4	24.5	50.1
Large farms :							
Denmark	155	824	779	32.3	0.4	16.1	...
Finland	72	310	383	36.4	5.0	26.8	14.6
Sweden	113	573	638	38.3	—	18.0	...

The figures in this table are subject to the limitations of such sample analyses and may not be wholly typical of farming enterprises in the countries mentioned, since the keeping of accounts usually indicates modern management. The actual qualifications and interpretations to which the figures are subject are detailed in the volume from which they are taken. They are sufficient, however, to indicate a very wide range of variation in the types of farming surveyed. It is notable, for example, that, where productivity is greatest, the amount of credit used is also greatest. Poverty of production and lack of credit go together. It is clear also that, even in 1928-29, actual returns were insufficient in most countries to provide what the farmer regarded as a fair return for his labour and current interest on the capital value of his equity, to say nothing of profit.

Unfortunately, it is not possible to give complete and

¹ Including assessed value of family labour, except in Netherlands.

² In the case of Netherlands, Norway and Sweden, depreciation charges are not separately shown.

³ Including assessed return on own capital.

⁴ At date when balance-sheet was closed — viz., January 1st, Austria and Czechoslovakia; March 1st, Switzerland; May 1st, Estonia and Latvia, and July 1st for all other countries mentioned.

comparable statistics for later years ; but the course of development in certain typical countries may be followed from other sources. A Danish investigation shows clearly the downward drift.

Agricultural Income and Expenses in Denmark. ¹

Year	Gross income Kr. per hectare	Net income Kr. per hectare
Average 1924-25 to 1928-29	902	104
1929-30	817	135
1930-31	656	13
1931-32	546	— 28
1932-33	509	— 43

One further example may perhaps be cited to show that debt problems are not confined to the newer countries. For Germany, the Institut für Konjunkturforschung has published statistics which may be summarised as follows :

Agricultural Income and Indebtedness in Germany. ²
RM. (000,000,000's.)

	1913	1929-30	1930-31	1931-32	1932
Farm indebtedness	17.5	11.4	11.6	11.8	11.4
Value of produce sold off the farm		9.86	8.69	7.3	6.5
Interest paid	0.75	0.95	0.95	1.01	0.85
Interest as a percentage of gross income		9.6	10.9	13.8	(13.1)

Other statistical estimates might be quoted to show the heavy and increasing burden of agricultural indebtedness in European countries. In Poland, for example, the total agricultural debt, which in 1930-31 represented about 25 per cent of the land value of small farms and 40 per cent of larger farms, increased between January 1931 and November 1932 from 4,000 to 4,600 million zloty. Assuming an average interest rate of 13 per cent, a 10 per cent increase of indebtedness is estimated to raise costs

¹ Landökonomische Driftsbureau : *Undersøgelser over Landbrugets Driftsforhold*, XIV. Copenhagen, 1931.

² *Statistiske Efterretninger*, January 5, 1933.

³ Institut für Konjunkturforschung : *Sonderheft 26*, pages 17 and 18 ; *Konjunktur Statistisches Handbuch*, 1933.

of production on small farms by 4 per cent.¹ In Yugoslavia, also, the total of agricultural debt is officially estimated to have risen from 1,500-2,000 million dinars in 1928 to 2,500-3,500 million dinars in 1931. Unofficial estimates are much higher.² In Italy, the agricultural indebtedness at the middle of 1932 was estimated at 9 to 10 milliard lire, while the gross farm income was 25 to 30 milliard lire, of which about 5 milliards went to landowners.³ The substantial decrease of interest payments in Germany draws attention to one of the most striking recent developments of the agricultural situation—the intervention of the Governments in order to reduce interest charges on agricultural debt.

✓ The variety and complexity of the measures taken by various Governments to relieve the agricultural situation cannot be described briefly. The far-reaching plans of the United States Government are summarised in the final chapter of this volume. In a great number of other countries, measures have been taken to postpone debt claims, give priority to new loans, convert short-term into long-term obligations, negotiate rent reductions, convert fixed money rents into yearly payments depending upon the value of farm produce, and grant tax relief. Illustrations of these measures may be drawn from both European and non-European countries. Thus, in Germany, a new "law for regulating agricultural indebtedness", passed in May 1933, enables debtors to appeal for special assistance in respect of debts entered into before July 13th, 1931. A bank, savings bank, or co-operative credit association chosen by the debtor can enforce arbitrary conversion of short-term into long-term debt at interest rates reduced to 4½ per cent, and, with the approval of the local courts (Amtgericht), reduce all claims except on first mortgages by as much as 50 per cent. Financial assistance is also provided by the Reich.

In the Netherlands, widespread advantage has been taken of the courts set up to negotiate between agricultural debtors and creditors, and compulsory interest reductions have taken place in Germany, Czechoslovakia, Poland and Latvia. In Denmark, extensive legislation was passed setting up county boards with power to postpone interest and amortisation payments, making provision for new loans and for moratoria on old loans, giving priority to new loans, taking powers to regulate production in pursuance of the new quota agreements, granting tax relief, limiting interest rates, facilitating mortgage conversions, creating a depression

¹ National Scientific Institute of Rural Economy at Pulaway, Economic Section of Small Farms.

² International Institute of Agriculture, "The Agricultural Situation 1931-32", Rome, 1933.

³ The Association of Italian Corporations' Business and Financial Reports, 1933.

fund with objects similar to those of the Reconstruction Finance Corporation in the United States, and allowing smallholders to convert their properties into State tenancies.¹ Another form of State assistance in force in the Scandinavian countries consists of the granting of new advances conditional upon prior agreements between debtors and creditors.²

It is clear that the impact of a severe depression which impairs the solvency of farm enterprises at once lessens farm credit and checks the flow of capital for agricultural uses. Measures to revive that flow by giving new loans priority over those formerly contracted strike a severe blow at the whole basis of agricultural lending. In many countries, either by legislation or by private contractual arrangements, efforts are now being made to change agricultural finance from a monetary to a commodity basis, both rent and interest being made payable as a share of the value of the annual produce. Such arrangements are now being made in a great number of European countries.

Even the scattered and incomplete evidence cited in this section is sufficient to show that, except in a few countries where agriculture is primarily dependent upon a protected domestic market, the depression has brought extreme difficulty to farming communities. It has not only reduced their current incomes, but, in the newer countries especially, has wiped out the accumulated profits of past years by greatly reducing the farmer's equity in the value of this land. Farm labour has shared in the distress, and the point has been reached where loans upon landed security are so burdensome that re-adjustments and writing-down have in many cases been inevitable. In the process of such writing-down, however, many countries find themselves faced with serious financial and banking difficulties. The Japanese peasant, the Indian producer of jute, the Brazilian coffee-grower, the Malayan rubber-planter, the Hawaiian sugar-grower, the New Zealand dairy-farmers, the cotton-planters of southern United States, are all facing the same problems of inelastic debt charges and record low prices. In face of shrinking incomes, they have made the same almost instinctive effort as their compeers in other lands to surmount their difficulties by increasing production, only to find their incomes shrink further as world markets narrowed and prices fell still lower. In agriculture, as in industry, profits have disappeared under the combined pressure of low prices and heavy fixed charges.

¹ *Oekonomi og Politik*, March 1933.

² International Institute of Agriculture, "The Agricultural Situation 1931-32", Rome, 1933.

Chapter VI.

THE STRAIN ON THE PUBLIC FINANCES.

THE EFFECTS OF THE FALL IN NATIONAL INCOMES.

The central fact concerning public finance during the depression has been the extraordinary difficulty experienced in adjusting public income and expenditure to greatly reduced national incomes. National incomes, using that term to mean the aggregate value of goods and services enjoyed by the whole community, have been considerably reduced in most countries, both in reality and still more in nominal value. The financial transactions of Governments have thus been rendered vastly more difficult. Expenditure has not been easy to reduce, and what reductions have been effected have often temporarily disturbed economic equilibrium. The incomes of Governments, derived largely from taxation, have fallen sharply. Old taxes have not only been affected by the lower income levels, but in some countries appear to have reached the point where further increases in rates are likely to bring a decline rather than an increase in yield. New and elastic sources of taxation have not been easy to find, and, where expenditure has not been easily reduced, a drift towards increasing indebtedness has been inevitable.

The *Survey* for 1931-32 contained estimates¹ of the percentage of national incomes expended by the State in several countries. The percentage naturally varied with the economic circumstances of the countries in question, but in each case had increased substantially as compared with the pre-war period. The statistics available seem to indicate that from one-fifth to one-fourth of the national incomes passed through the Government (including local authorities) budgets.²

National incomes have now decreased very substantially, after a long period during which they had increased rapidly

¹ Page 247.

² See also Statistisches Reichsamt, "Internationaler Steuerbelastungsvergleich", *Einzelchriften zur Statistik*, Nr. 23, page 646.

with only few and brief interruptions. From 1890 to 1914, for example, there was no single year in which the German¹ or Japanese² estimates of national income declined, and, while the trend was not so regular in other countries, it was quite definitely upward. After the war, this trend appeared to be resumed, and even the sharp declines caused by the crisis of 1920-21 were quickly restored. Except in those European countries which had been impoverished by the war and subsequently by inflation, the post-war standard of living was not only higher, but appeared to be improving more rapidly, than in the pre-war period. The immediate post-war crisis of 1920-21 was overcome comparatively quickly. The fall in national income in that crisis was probably greatest in the United States of America, where it was 14 to 15 per cent.³ By 1925, in practically every country, this setback had been made good.

The fall of national income in the present depression has been much greater. A recent estimate for the United States shows a decline of 53 per cent between 1929 and 1932.⁴ In Germany, an estimate for the same period is 39 per cent,⁵ and in the United Kingdom 20 per cent.⁶ Between the years 1928 and 1931, the national income of Australia is estimated to have fallen by 33 per cent;⁷ the figure for New Zealand was also 33 per cent;⁸ for Roumania 36 per cent.⁹ The decline continued in 1932, bringing the Roumanian figure, for example, up to 53 per cent. For the shorter period from 1929 to 1931, the fall was 10 per cent in Norway,¹⁰ and in Italy 33 per cent.¹¹ The Welder Commission, which reported upon the financial condition of the Netherlands in 1932, regarded 30 per cent as a very moderate and optimistic estimate of the decline in taxable income since 1929.¹² The value of the gross production fell from 1926 to 1932 in Chile from 3,200 million pesos to 2,200-2,400 million, or about 30 per cent,¹³ in spite of a depreciation of the currency of about 50 per cent.

¹ Statistisches Reichsamt *Einzelchriften zur Statistik*, Nr. 24, "Das deutsche Volkseinkommen vor und nach dem Kriege".

² Institut international de Statistique, XXV, 2, Tokyo, 1930.

³ King "The National Income", New York, 1930.

⁴ *National Industrial Conference Board Bulletin*, February 20th, 1933.

⁵ Institut für Konjunkturforschung, "Vierteljahrsheft", 7. 4. A.

⁶ Clark: "The National Income, 1924-1931", *Economic Journal*, June 1933.

⁷ "Report of the Committee appointed to make a Preliminary Survey of the Economic Problem", April 1932.

⁸ *Canterbury Chamber of Commerce Bulletin*, April 1933.

⁹ *Buletin Trimestrial al Institut Roumanesc de Conjunctura*, 1933, 1 and 2.

¹⁰ *Statistiske Meddelelser*, Nr. 10-11, 1932.

¹¹ The Association of Italian Corporations, "Business and Financial Report", June 1st, 1932.

¹² Rotterdamsche Bankvereeniging, *Monthly Bulletin*, November 1932.

¹³ *South American Journal*, January 28th, 1933.

The dilemma presented to those responsible for the public finances by such great declines in the national income of almost every country arises mainly from the inflexibility of public expenditure in face of declining revenue. While adequate statistics are not available to measure recent tendencies, it is clear that the percentage of national incomes taken for purposes of State has sharply increased. The obvious counterpart of this increase is a great shrinkage of the resources available for private consumption and the provision of industrial capital. If Government receipts before the depression were one-fifth of the total national income, and the national income has since fallen about 40 per cent while Government receipts have remained almost constant, these should now represent almost 33 per cent of the total national income, and the share remaining in private hands would thus have fallen by one-half. Since standards of consumption are difficult to reduce, most of the shrinkage has been concentrated upon the amounts available for the provision of new capital equipment. The strain upon the public finances has been a powerful deflationary factor in the present depression.

Moreover, as will be shown later in this chapter, very important changes in the methods of providing capital equipment seem likely to result from the difficulties of private investors in finding employment for their capital on the one hand and the necessities of Governments on the other. There is a distinct trend in a number of countries towards the promotion of capital expenditure by Governments, as a means of securing relief from prolonged unemployment and generally as a means of escape from the spiral of deflation. Such expenditure at present is necessarily made from funds provided by adding to governmental indebtedness, so that the direction and control of investment tends in such cases to pass from private to public initiative.

In attempting to analyse the most recent developments of public finance in important and typical countries, there are unusual difficulties at such a time as the present. Brief reference was made in the preceding *Survey* to some of the more important technical difficulties presented by any scientific study of public finances.¹ The published statements upon which current discussion is usually based need a great deal of detailed analysis and interpretation and usually require a great amount of supplementary information before any reliable estimate can be formed of the true financial position of any particular country. Public accounts are extremely complicated, and those which are most commonly discussed cover only a part of the total receipts and expenditure of Governments. Even if the whole position

¹ *World Economic Survey, 1931-32, pages 245-248.*

were finally revealed by a laborious investigation of all the different accounts, both of central and local Governments and of the semi-detached governmental enterprises and participations, it would be still necessary to consider both the monetary and the general economic situation of the country in question before a true estimate of its financial position could be arrived at. International comparisons offer so many additional complications as to render simple statements extremely unreliable and misleading. Pre-eminently, the problems of public finance constitute a series of national problems to be considered in the light of the economic circumstances of each particular country.

In the discussion which follows, it is impossible to attempt any complete picture either of the problems of single countries or of the international aspects of public finance. It is, of course, a truism that the fall in national incomes which lies at the root of the financial difficulties of so many Governments is largely caused by economic and financial factors which are common to most countries. The fall in prices, declining international trade, currency instability, the burden of excessive debt and international economic disequilibria generally are the central factors of the whole depression. But the methods by which Governments have faced the fall in national incomes vary so greatly that, whatever the ultimate causes of strain may be, public finance becomes primarily a domestic problem.

The most recent developments of public finance are rendered more difficult of analysis by the fact that closed accounts giving a picture of what has actually happened are not yet available in most cases, and will not be available for a considerable time. Final conclusions must be left to future economic historians. The best that can be achieved at the present time is a study of some of the outstanding factors in the situation of important countries as disclosed by the information now available. On the pages which follow, therefore, an attempt is made to single out important recent phenomena and to give illustrative examples drawn from typical cases, rather than to provide either a complete summary or a considered estimate of the total development.

Even this limited task is complicated by the fact, inevitable in such a period of strain, that there have been considerable but subtle changes in the presentation of public accounts. Everyone is familiar with the devices to which individuals are forced at periods of financial embarrassment in order to provide for current necessities. Transfers of resources between different accounts, delayed payments, temporary advances, suspension of commitments and similar devices are both inevitable and legitimate in an emergency; but they greatly increase the difficulty of analysis.

DECLINING PUBLIC REVENUES.

In more normal times, when there is a greater measure of private and public prosperity than the world has enjoyed in recent years, the logical approach to any analysis of public finance is by way of expenditure.

But the sources of both the public and private expenditure are the same, and prudent Governments, even in times of prosperity, keep in mind the political and economic limits of taxable capacity. As long as prosperity is general and revenue is therefore buoyant, no more than ordinary prudence is required. When prosperity has given way to widespread depression and revenues are heavily declining, expenditures can no longer be calculated with merely ordinary prudence. In such circumstances, Governments, like individuals, must adjust their notions of necessary expenditure and consider their budgets from the side of revenue. There are at the present time an increasing number of countries where this readjustment of budgetary procedure has been pushed very far. The most powerful financial countries may still maintain "necessary" expenditures either by increased taxation or by borrowing, but even they have greatly revised their definition of what is "necessary". In many poorer countries, the revision has reached the point where expenditures are allocated for periods as short as a month, after consideration of the resources likely to become available in those periods. The available revenue rather than the expenditure necessary has been the decisive factor in financial policy.

The decline in public revenues during recent years is somewhat disguised by the fact that rates of taxation have been increased, new taxes introduced and methods of collection tightened in many countries. Even when individual taxes are considered, these changes obscure the real position. Some indication of the extent to which Treasury problems have been complicated by the depression may perhaps be gained by recalling some of the statistical estimates contained in preceding chapters of this volume. For example, the total value of world imports fell in 1932 to less than 40 per cent of what it had been in 1929. In many countries the fall was much greater, ranging up to 87 per cent. The decline of Customs revenue was, of course, affected by the imposition of new Customs duties and the increase of existing rates, and it is reasonable to suppose that free imports fell off less than dutiable imports. The decline in Customs receipts might, according to circumstances, have been greater or less than it actually was, if no alteration had been made in tariff schedules. On the other hand, the direct taxation of

individual or corporate incomes would have yielded much lower results than they actually did, both because the average incomes were lower and because a much larger proportion fell within the lower scales of graduation, if rates had not been raised, graduated scales revised, exemptions lowered, allowances reduced and methods of collection improved. When such factors are borne in mind, the declining yields of taxation illustrated below are very significant.

Receipts from Customs Duties, 1929-1932.
National currencies (000,000's).

Country	Currency	Tariff level index in 1925 ^a	Financial year				1932 as a percentage of 1929
			1929	1930	1931	1932	
Netherlands ¹	Gulden	4	72	71	67	83	115
United Kingdom ²	£	4	120	121	136	167	139
Denmark ²	Kr.	6	102	108	105	84	82
Belgium ¹	Franc	8	1,319	1,336	1,303	1,556	118
Switzerland ¹	Franc	11	277	306	315	322	116
France ²	Franc	12	4,449	4,785	5,921	4,139 ⁵	...
Germany ²	RM.	12	1,095	1,083	1,147	1,106	101
Austria ¹	Sch.	12	286	290	267	230	80
Sweden ²	Krona	13	154	154	148	138	90
India ³	Rupee	14	513	468	...	...	...
Canada ²	\$	16	179	131	104	...	...
Italy ²	Lira	17	3,042	2,427	2,983	2,452	80
Czechoslovakia ¹	Koruna	19	1,387	1,195	1,289	863	62
Hungary ³	Pengö	23	125	97	80	50	40
Poland ¹	Zloty	23	395	258	157	135	34
Australia ²	£A	25	29.5	30.2	18.2	18.6	63
Argentina ¹	m \$ n	26	424	355	313	286	67
United States ²	\$	29	603	585	378	328	54
Spain ¹	Peseta	44	665	580	497	528	81

The importance of Customs duties in almost every budget is due, not only to the aggregate of the revenue so collected, but to its elasticity. Additional duties upon imports have always been one of the first lines of reserve upon which Ministers of Finance may call in an emergency. This fact lends additional interest to the statistics quoted above. The countries concerned have been arranged in order of the approximate relative height

¹ Financial year beginning January 1st.

² Financial year beginning April 1st.

³ Financial year beginning July 1st of preceding year.

⁴ League of Nations "Tariff Level Indices" (Method B1).

⁵ Nine months only; the figure for the same nine months in 1931 was 4,609.

of their tariff levels in 1925,¹ and the greater elasticity of revenue in the low-tariff countries is obvious. With one exception (Denmark, where trade regulation was attempted by exchange control rather than by raising the tariff), the low-tariff countries have managed to increase the yields from Customs taxation. Where the tariff rates were highest, on the other hand, the shrinkages of revenue, despite very considerably increased duties in many of the countries concerned, suggest that the limits of taxable capacity are being reached or exceeded. Further increases in rates in these countries bring a decline rather than an increase in revenue, at least in present circumstances.

Receipts from Income Taxation 1929-1932.
National currencies (000,000's).

Country	Currency	Financial year					1932 as a percentage of 1929
		1929	1930	1931	1932	1933	
Australia ⁴	£A	9.8	11.1	13.6	13.5	10.0*	138
Austria ² :							
Income tax . . .	Sch.	182	181	159	135*	...	
Corporation tax	Sch.	96	79	69	45	...	47
Canada ²	\$	69	71	61	...	...
Czechoslovakia ² .	Koruna	1,431	1,161	1,061	1,020*	...	
Denmark ²	Kr.	68	69	89	62*	...	
France ²	Franc	14,101	13,587	11,901	...	...
Nine months only	Franc	...	...	10,238	7,518	...	62
Germany ² :							
Income tax . . .	RM.	3,026	2,761	2,143	1,333	...	44
Corporation tax	RM.	559	450	304	106	...	19
India ³	Rupee	167	160	173*	187*	...	
Italy ⁴	Lira	3,995	3,754	3,296	2,935*	...	
Japan ²	Yen	200	201	164*	131*	...	
Netherlands ² . . .	Gulden	87	93	92	78	...	90
New Zealand ² . . .	£NZ	3.5	4	4.4	3.4*	...	
Sweden ⁴	Krona	145	151	164	151	134*	104
United Kingdom :							
Income tax . . .	£	237.4	256.1	287.4	251.5	...	106
Super-tax	£	56.4	67.8	76.7	60.7	...	108
United States ⁴ . .	\$	2,331	2,410	1,860	1,057	1,100*	45

* Budget estimates.

¹ Cf. League of Nations "Tariff Level Indices", Geneva, 1927. There were, of course, considerable alterations of tariffs between 1925 and 1933, and it is possible that the order of the individual countries has changed.

² Financial year beginning January 1st.

³ Financial year beginning April 1st.

⁴ Financial year beginning July 1st the preceding year.

⁵ General income tax, scheduled income tax, land tax and income tax on movable property.

⁶ Income tax on movable wealth and super-tax on income.

⁷ Including tax on capital.

The even stronger tendency towards a declining yield from direct taxation is not as easy to illustrate and does not offer the same opportunity for international comparisons ; but the income-tax statistics for certain countries may be used to give a rough indication of the decline. There is always a lag before reduced incomes are reflected in reduced tax yields, but the table on page 167 makes it clear that by the financial year 1932-33 the effects of the depression were being fully realised. The nature and effectiveness of income taxation differs in the countries cited, so that comparisons are invalid. In all there was a definite tightening up of collection methods, and in most the rates and graduation scales were increased at the same time as exemptions were reduced and allowances revised. Nevertheless, the yield fell in the great majority of cases.

Certain additional comments may be made on these figures. The increased revenue shown for the United Kingdom in the financial year 1931-32 was due to the rate being raised from 4s. 6d. to 5s. in the £, and also to the payments being anticipated, so that a greater amount was brought into the receipts of that year. The budget for 1933-34 made certain adjustments in the methods of collection, but did not lower rates. The estimated revenue from income tax in 1933-34 is £229 million and from super-tax £51 million.

In Germany, it will be noticed that the decline in income-tax receipts was more than 50 per cent between 1930 and 1932. This is all the more remarkable because so large a proportion of the tax is deducted from wage and salary payments, which fell from 1,281 million RM. to 745 million RM. The fall in the income tax levied upon incomes from capital investment was from 194 to 45 million RM., a proportion very much closer to that of the decline in the yield from corporation taxes.

The importance of the decline in these major sources of indirect and direct taxation may be gauged by the following table, showing the proportions contributed by various forms of taxation to the total revenue collected by certain countries in 1927-28.

It is obvious that, in face of such heavy declines in the yield from major sources of taxation, great efforts have been necessary to increase the yield from other sources and to devise new methods of taxation. Inevitably there has been a considerable increase in indirect taxes levied upon turnover or consumption, together with new forms of direct taxation in many countries, such as levies upon wages. The effect of increased Customs protection in diverting consumption to domestic products strengthens the tendency for revenue to be sought by taxation of the domestic industries. Despite the increasing rates of new and old taxes,

*The Principal Sources of Tax Revenue in 1927-28.*¹
(As percentages of total taxation.)

Country	Customs receipts	Taxes on income and property ²	Taxes on transfer and turnover ³	Taxes on consumption ⁴
Australia	53	26	—	21
Austria	20	30	25	25
Belgium	11	35	40	13
Bulgaria	30	23	14	33
Canada	43	16	21	19
Czechoslovakia	13	22	27	31
Denmark	25	35	6	35
Finland	57	23	11	9
France	6	34	33	23
United Kingdom	16	57	4	24
India	66	20	0.4	15
Italy	20	40	19	22
Japan	12	33	9	44
Netherlands	11	45	9	35
Norway	36	31	2	28
Poland	16	30	8	42
South Africa	44	42	5	10
Spain	19	30	17	30
Sweden	25	27	11	37
Switzerland	68	13	17	2
Turkey	21	19	6	55
United States	18	67	1	14

there has been a disconcerting decline in the budget receipts. The table on page 170 shows that, in the case of the United States, this decline amounted to more than 45 per cent. Since in one country only among those cited (Belgium in 1930) were there any substantial remissions of taxation in this period, the fall in revenue is wholly due to declines in taxable capacity.

¹ Statistisches Reichsamt : *Finanzen und Steuern*, pages 842-847.
² Including death duties, with the exception of Poland.
³ With the exception of Poland, excluding death duties.
⁴ Including net yield of monopolies.

Budgetary Receipts in Certain Countries, 1929 to 1932.
(Excluding proceeds of loans.)
National currencies (000,000's).

Country	Currency	Financial year				
		1929	1930	1931	1932	1933
Austria ¹	Sch.	2,010	2,027	2,009	1,905 *	...
Canada ^{2 4}	\$	441	350	330	...	...
France ²	Franc	47,780	45,681	43,102	28,882 ⁵	...
Germany ²	RM.	10,641	10,655	8,953	7,382	...
Hungary ³	Pengő	1,483	1,480	1,464	1,229	1,207*
Italy ^{3 6}	Lira	21,654	20,198	20,545	18,317	18,895*
New Zealand ²	£NZ	25.3	23.1	21.2	19.1*	...
Poland ²	Zloty	3,029	2,750	2,262	2,002	...
South Africa ⁴	£SA	30.5	28.5	27.0	29.4*	...
Spain ¹	Peseta	4,225	3,735	3,656	3,886	...
Sweden ³	Krona	738	784	791	806	795*
Switzerland ¹	Franc	396	433	428	420	...
United Kingdom ²	£	815	858	852	827	...
United States ²	\$	4,036	4,174	3,319	2,118	2,624*

THE ADJUSTMENT OF PUBLIC EXPENDITURES.

The greater part of the chapter devoted to public finances in the *Survey* for 1931-32 was concerned with the inflexibility of governmental expenditures in the early stages of the depression. It is on the side of expenditure, however, that statistical material concerning public finance is most unsatisfactory and most delayed, so that there is no possibility yet of getting anything like a complete picture of the most recent expenditures in a number of important countries. Closed accounts are the exception rather than the rule for the year just past, and in the discussion of expenditure which follows, therefore, an attempt is made only to draw attention to a few salient developments in recent months.

In the previous *Survey*, attention was focused upon three main groups of expenditure — debt service, armaments, and social services — which seemed of special importance by reason both of their magnitude and of their social and economic significance. Little can be added in this *Survey* to that discussion,

* Budgetary estimates.

¹ Financial year beginning ~~July 1st.~~ *January 1st.*

² Financial year beginning April 1st.

³ Financial year beginning July 1st of preceding year.

⁴ Consolidated revenue fund only.

⁵ Nine months only. The corresponding figure for the first nine months of 1931 was 13,587 million francs.

⁶ Payments including those from preceding years, not including issue of coinage.

since new information for the years 1931-32 and 1932-33, during which the strain on national budgets caused real reductions of expenditure, is still scanty and incomplete. There is no reason to repeat here the description of the manner in which these important groups of expenditure developed after the war, but the information already available for the years 1931-32 and 1932-33 is sufficient to suggest certain additions to that description.

The first fact to be noted is that the sharp declines of revenue previously noted, together with an increasingly dangerous budgetary position in most countries, finally forced a reconsideration of expenditures. As the table which follows will indicate, effective reductions were not applied in most cases until the fiscal years 1931-32 and 1932-33. Up to that time, revenue had benefited by the delayed returns, for example, of income tax, reflecting the years of prosperity; and the depression in any case had not reached the depths to which it afterwards fell. At the same time, governmental schemes to combat the depression and relieve distress seemed more feasible and, in addition, there was a general reluctance to cut important services. The depression entered a second stage, however, with the onset of financial panic in May 1931, and in that second stage the controversies concerning public expenditure as a means of remedying the depression became acute. Before entering upon a discussion of the way in which various Governments have attempted to meet this new situation, it is necessary to tabulate the available information concerning public expenditures. The figures below need to be read in the light of the explanations given in the footnotes. They refer only to expenditures which are included in the general budgets of the central Governments, and not to expenditures included in special budgets, such as exist in many countries for trading enterprises, works and other purposes.

The figures shown in the table are comparable horizontally, but not vertically. Methods of accounting, the proportion between public and private economic activity, and the proportions between the activities of central, regional, local and other public bodies vary greatly from country to country.

The figures in most cases represent estimated or actual cash disbursements, but in some cases they represent pay warrants issued, commitments, or even credits which may be drawn on in subsequent years. The main purpose for which the table is included here is to indicate the general trend of development; if it is desired to utilise particular figures, the table should be supplemented by the more detailed statistics available in the *Statistical Year-Book*, 1932-33.¹

¹ Table 109.

Budgetary Expenditure of Central Governments, 1929 to 1933.
(Amortisation expenditure included.)
National currencies (000,000's).

Country	Currency	1929 1929-30	1930 1930-31	1931 1931-32	1932 1932-33	1933 1933-34
Argentina . . .	m \$ n	...	1,095	886	839	...
Australia . . .	£A	104	104	98	...	...
Austria . . .	Sch.	1,990	2,289	2,331	1,920	1,932*
Chile . . .	\$	1,596	1,131	1,027	597	...
China . . .	S Ch.	539	714	683	...	...
Colombia . . .	Peso	82.2	60.1	47.6	34.8*	40.4*
Czechoslov. . .	Koruna	10,275	9,928	12,260	9,319*	8,633*
France . . .	Franc	63,968	53,265	50,641*	41,098*	...
Germany . . .	RM.	11,353	11,740	9,555	8,219*	...
Greece . . .	Drachma	18,363	11,180	11,280	8,674*	...
India . . .	Rupee	...	1,362	1,344*	1,278*	...
Italy . . .	Lira	20,790	25,702	20,164*	20,923*	...
Japan . . .	Yen	1,736	1,558	1,498*	1,944*	...
Mexico . . .	Peso	276	279	299	215	...
Netherlands . .	Gulden	909	839	880*	1,116*	...
Poland . . .	Zloty	2,993	2,813	2,866*	2,452*	2,458*
Spain . . .	Peseta	4,056	3,697	3,855	4,470	...
Sweden . . .	Krona	811	819	894	896*	...
United Kingd. .	£	840	881	860	848*	...
United States .	\$	3,994	4,231	5,007	4,269*	3,975*

* Budgetary estimates.

Argentina: The budget includes expenditure on public works and armament material, covered from loans issued, amounting for 1930 to 207.2 million, for 1931 to 102.5 million and for 1932 to 61.9 million pesos.

Australia: Consolidated Revenue Fund only. Expenditure from Loan Funds amounted in 1930-31 to £71.5 million.

Austria: 1933; revised estimates.

Chile: Ordinary budget only; extraordinary expenditure amounted to 535.1 million and 225 million pesos for 1930-31 and 1931-32, respectively.

Colombia: Ordinary and extraordinary budgets; for 1932, ordinary budget only. Expenditure of closed accounts represents actual payments.

Czechoslovakia: Not including special funds.

France: Not including the Amortisation Fund (deriving its receipts from the net yield of the Tobacco Monopoly, the yield of transfer taxes, succession duties, etc.) or special accounts. Closed accounts: provisional results according to the situation of the Treasury on the basis of *Comptes d'exercice*. The budget year 1929-30 covers a period of fifteen months, the budget for 1929 having been prolonged for the three months January to March 1930. The budget year 1932 covers a period of nine months.

Greece: The high expenditure figure for 1929-30 is accounted for by the fact that the proceeds and utilisation of various loans, which were not formerly entered in the budget accounts, have been entered in those for 1929-30.

India: The figures relate to the Revenue Account only and exclude the expenditure on irrigation, postal and telegraph services and other capital outlay not charged to revenue, permanent public debt discharged and loans and advances by the Central Government, which — with the exception of a small amount of reimbursements — are covered from fresh loans. The expenditure under the above-mentioned headings amounted to the aggregate sums of Rs. 482.2 million for 1930-31, Rs. 589.9 million

Continued at foot of next page.

This first table does not give a clear picture of the contraction of real expenditure, because amortisation expenses, which fluctuate considerably from one year to another, are included.

In the table given below, the amortisation expenditure has been deducted and the figures give a clear impression of the contraction of real expenditure.

Budgetary Expenditure of Central Governments, 1929 to 1933.
(Amortisation expenditure excluded.)
National currencies (000,000's).

Country	Currency	1929 1929-30	1930 1930-31	1931 1931-32	1932 1932-33	1933 1933-34
Austria	Sch.	1,922	2,213	2,249	1,888*	1,859*
Czechoslovakia	Koruna	9,411	9,484	11,776	8,769*	8,242*
Germany	RM.	10,976	11,006	8,874	7,568*	...
Greece	Drachma	17,042	9,883	10,289	8,650*	...
India	Rupce	...	1,300	1,275*	1,210*	...
Italy	Lira	20,458	21,468	19,644*	20,690*	...
Japan	Yen	1,456	1,285	1,238*	1,684*	...
Netherlands	Gulden	747	863	802*	750*	...
Poland	Zloty	2,877	2,715	1,761	2,346*	2,330*
Sweden	Krona	770	787	855	888*	...
United Kingdom	£	792	814	827	815*	...
United States	\$	3,440	3,791	4,594	3,771*	3,240*

* Budgetary estimates.

Inspection of the figures shows that, while estimates only are available in a great many cases and actual expenditure is apt to be greater than estimated, there was an unmistakable downward trend of expenditure in the years 1931 and 1932. The exceptions to this general rule are China, Japan, Spain, Italy, Sweden and the U.S.S.R. Of these countries, China is on a silver standard, with rising price-levels, and has had to

(estimated) for 1931-32 and Rs. 453.6 million (estimated) for 1932-33.
Figures for 1931-32: revised estimates.

Italy: Expenditure figures refer to estimated or actual commitments (engagements).

Japan: Excluding special accounts. Amortisation figures represent amounts transferred to National Debt Consolidation Fund.

Netherlands: Including Loan Redemption Fund and Road Fund. Amortisation includes, in 1929, 100 million gulden, and, in 1932, 299.5 million of extraordinary amortisation.

Poland: 1933-34 budget includes net receipts and net expenditure of special funds, forming a special chapter of the budget.

United Kingdom: Excluding capital expenditure authorised by various Acts, amounting, for 1930-31, to £11.3 million and for 1931-32 to £9.7 million.

United States: Figures refer to General Fund, Special Funds and Trust Funds. Amortisation, 1933-34: includes \$200 million extraordinary amortisation due to estimated repayments from Reconstruction Finance Corporation.

face extraordinary military expenditures. Japan also has had military expenditure and a depreciating currency. In Spain there has been a change of regime. In Italy, the corporative State is so managed as to render the maximum of support to industry in difficult times. In Sweden, the expansion of expenditure has been the result of deliberate policy directed towards a removal of the depression by investment expenditure in the manner described later. The estimates for the U.S.S.R. are in roubles and show a steady increase from year to year.

ARMAMENT EXPENDITURES.

When attention is directed to the particular manner in which expenditure has been reduced, statistics are very scattered; but certain items of information, positive and negative, are available. The table below is summarised from the *Armaments Year-Book*, 1933. The statistics are given in national currencies to emphasise the fact that they are not directly comparable.

Expenditures on National Defence, 1929-30 to 1933-34.
National Currencies (000,000's).

Country	Currency	1929 1929-30	1930 1930-31	1931 1931-32	1932 1932-33	1933 1933-34
Australia . . .	£A	4.4	3.7	3.1	2.9*	...
Belgium . . .	Franc	981	1,216*	1,404*	1,052*	...
Bolivia . . .	Boliviano	9.2	8.7*	9.3*	...	...
Brazil . . .	Milreis	445	490	411	416*	496*
Bulgaria . . .	Leva	1,078	1,036	1,054*	982*	...
Canada . . .	SC	21	23	18	14*	14*
Chile . . .	Peso .	237	209	165	125*	...
China . . .	\$(silver) (Yuan dollar)	245	312	304	...	...
Cuba . . .	Peso	12.7*	12*	10.1*	9.8*	...
Denmark . . .	Krone	50	46	45	43*	...
Estonia . . .	Kr.	18	18	16	16*	...
France . . .	Franc	10,969	11,600	12,022*	9,965*	11,910*
Germany . . .	RM.	691	681	617	678*	...
United Kingd.	£	99	95	92	89*	93*
India . . .	Rupee	504	495	471*	425*	...
Italy . . .	Lira	5,016	5,644	5,208*	5,194*	...
Japan . . .	Yen	495	443	407*	659*	...
Netherlands .	Gulden	75	77	79	73	65*
Poland . . .	Zloty	866	778	763	840*	829*
Spain . . .	Peseta	1,003	889	906	771*	...
Sweden . . .	Krona	138	130	125	122*	102*
United States.	\$	701	699	702	663*	616*

* Budgetary estimates.

PAYMENTS ON ACCOUNT OF PUBLIC DEBT.

Great changes are taking place in the expenditure for debt service in the various countries ; but it is impossible to summarise these changes in simple formulæ. The circumstances of every country are different. From the incomplete table printed in the following section, it will be seen that, in most countries, the total amount of public debt tends to increase, in some cases quite heavily. This is inevitable in a period during which revenues have fallen and expenditures have been difficult to reduce. But there are great changes in the distribution of the debt — for example, as between long- and short-term and as between foreign and domestic debt. These changes obviously alter the budgetary position, since they affect the annual cost of debt service, which is the most important practical consideration.

It is the actual payments on account of debt service in each year which are most significant, and the tables on page 176, reproduced from the League of Nations *Statistical Year-Book*, 1932-33, summarise the information available on this point for a number of typical countries.

As in the preceding tables, the main purpose for which these figures are given is to indicate the general trend. If it is desired to examine more closely the position of any particular country, it is essential that the more detailed statistics and explanatory footnotes contained in the *Statistical Year-Book*, 1932-33,¹ should be consulted. This caution applies particularly to the division made between interest payments and amortisation. The statistics given below include, as far as possible, the total amount of service corresponding to the outstanding debt, but in many cases they include only the charges upon the budget and not the expenditure effected by means of special funds. In most cases they include the allocations to sinking funds, not the redemptions effected by those funds. Where debts have been converted, the amount converted is shown under redemption, except where floating debt has been repaid by raising other floating debt.

There are great difficulties in interpreting the table, however, and, even with the definitions and qualifications given in the *Statistical Year-Book*, it must be used with the greatest possible caution. All the figures are taken from the official accounts of the countries concerned ; but, in the present circumstances of fluctuating exchange rates, controversies concerning the gold clauses in debt contracts, moratoria, suspensions of amortisation

¹ Table 110.

*Annual Debt Service (Interest and Amortisation Payments) of
Certain Countries, 1930 to 1933. National currencies (000,000's).*

Country	Currency	1930-31		1931-32	
		Interest	Amortisation	Interest	Amortisation
Argentina	Peso	232.0		241.3*	
Austria ¹	Sch.	88.8	74.9	125.0	81.7
Australia	£A	58.2	7.9	58.1*	
Brazil	Milreis	654.2*		782.6*	
Canada	SC	121.3	3.7	121.2	3.3
Czechoslovakia	Koruna	1,800.0	633.5	1,608.1	941.7
France ¹	Franc	13,194.9*		10,946.4*	
Germany ¹	RM.	248.1	734.2	253.0	681.1
Hungary	Pengö	54.6	53.9	53.0*	34.9*
India ¹	Rupee	503.4	61.5	535.5*	68.9*
Italy ¹	Lira	4,603.1	4,233.7	4,512.9*	520.4*
Netherlands ¹	Gulden	99.7	76.7	96.3*	78.0*
Norway	Krone	83.7	38.2	83.4*	27.1*
Poland	Zloty	165.7	98.9	210.4*	104.7*
Portugal	Escudo	440.4*		296.4*	
South Africa	£S.A.	10.5	1.0	10.3	0.7
Sweden	Krona	82.4	31.9	81.3	38.6
Switzerland	Franc	109.9	19.9	97.0	41.5
United Kingdom	£	291.9	66.8	287.6	32.5
United States ¹	\$	610.8	440.1	599.3	412.6
U.S.S.R. ¹	Rouble	257.2	207.2	287.8	120.5
Yugoslavia	Dinar	1,016.9*		1,220.3*	
		1932-33		1933-34	
Argentina	Peso	296.1*			
Austria ¹	Sch.	116.3*	76.4*	119.4*	72.1*
Australia	£A	51.7			
Brazil	Milreis	802.7*		693.8*	
Canada	SC	134.0*	3.5*		
Czechoslovakia	Koruna	1,599.0*	561.7*		
France ¹	Franc	9,168.4*	(9 mths)		
Germany ¹	RM.	286.7*	651.4*		
Hungary	Pengö	62.1*	35.6*		
India ¹	Rupee	548.2*	68.2*		
Italy ¹	Lira	4,836.3*	233.5*		
Netherlands ¹	Gulden	86.9*	366.2*		
Norway	Krone	89.3*	32.1*		
Poland	Zloty	169.7*	106.1*		
Portugal	Escudo	353.7*			
South Africa	£S.A.	10.9*	0.7*		
Sweden	Krona	91.7*	8.0*		
Switzerland	Franc	90.2*	41.3*		
United Kingdom	£	276.0*	32.5*		
United States ¹	\$	695.0*	498.1*	725.0*	734.0*
U.S.S.R. ¹	Rouble	1,000.0		1,330.0	
Yugoslavia	Dinar	1,558.7*		...	

¹ For footnotes, see following page.

and interest payments, defaults and transfer difficulties, it is all but impossible to compile statistics which will give an accurate description of the true situation. This is particularly the case regarding that portion of the public debt services payable in foreign countries. For example, the interest and capital repayments from such a country as Australia are payable partly on account of domestic debt, the interest on which has been reduced by a great conversion operation in 1932, partly on account of debt originally contracted in London and New York, mainly in terms of sterling. In January 1931, the exchange rate on London dropped from 10 per cent to 25 per cent below sterling, and when the United Kingdom abandoned the gold standard the Australian currency was still kept at 25 per cent below sterling. It is obvious, therefore, that the amount in Australian currency necessary to discharge the debt service payable in sterling has been considerably increased.

The Australian case is comparatively simple, but illustrates the necessity for close study of the particular circumstances of each individual country. When the much greater complexity of the debt and transfer situation — for example, in many European countries — is considered, the necessity for detailed studies in each particular case becomes more obvious.

Very important adjustments of debt service are in process. Some of the elements in that process can be mentioned, but it is impossible as yet to ascertain their ultimate effects. It is too soon even to judge whether the net results of conversions, interest reductions, compositions and defaults on the one hand,

* Budgetary estimate.

¹ *France* : Budgetary charges only, excluding service effected by Amortisation Fund and by Treasury.

Germany : Debt service incomplete, as it excludes : (1) service of foreign loan, 1924 (interest and amortisation indistinguishable) : 87 million RM. in 1930-31 ; 80.4 million in 1931-32 ; 79 million (estimated) for 1932-33 ; (2) service of 5 ½ % International Loan, 1930 : 79 million RM. (estimated), 1932-33.

India : Foreign debt in sterling has been converted at the rate of 1 rupee = 1s. 6d.

Italy : Amortisation, 1930-31 : chiefly conversion of seven-year and nine-year Treasury bonds into 5 % consolidated (Littorio) debt and nine-year Treasury bonds. Diminution in amortisation, 1932-33, is due to non-provision for payment to Amortisation Fund on account of domestic debt ; corresponding estimate for 1931-32 : 300 million lire.

Netherlands : Amortisation, 1932, includes extraordinary amortisation, 299.5 million gulden.

United States : Amortisation, 1933-34, includes extraordinary amortisation of \$200 million due to estimated repayments by Reconstruction Finance Corporation.

Union of Soviet Socialist Republics : Figures under 1930 (1930-31) refer to 1929-30 (October 1st to September 30th). Following figures refer to calendar year.

and the contracting of new debt on the other, will raise or lower the future burden of public indebtedness. Each country must in this respect be considered separately. But it seems clear that, in strong financial countries such as the United Kingdom, Belgium, the Netherlands, and also in several of the British Dominions and in India, where there has been firm control over the public finances, the ultimate result of the cheapening of interest rates is likely to be a considerable relief to future budgets. There has been budgetary relief also from compulsory reductions of domestic interest rates in many countries, including Australia, Bulgaria, Czechoslovakia, Germany, Greece, New Zealand and Poland. Apart from the relief given directly to the budgets, the lowering of the interest upon other forms of lending tends to make Government finance easier. This relief should be clearly distinguished from that gained by temporary suspensions of sinking funds and amortisation payments, which, however justifiable in an emergency, merely postpone the payments due and spread them over a longer period, with some ultimate increase in total cost. The position is not yet clear in France, where in the earlier phases of the depression it was possible to continue the policy of reducing foreign debt and also to convert part of the domestic debt. Subsequent budgetary difficulties, however, have caused an increase in the floating domestic debt and have prevented any further conversions.

In a great many other countries, including such strong financial Powers as the United States, the weaker budgetary position may result in substantial increases of debt service.

As against this tendency for domestic debt to increase wherever recent budgets have not been brought into equilibrium, there must be placed the reductions of debt service in many countries which have been unable to launch fresh loans on either the domestic or the foreign market.

INVESTMENT EXPENDITURES AND PUBLIC WORKS.

From the foregoing discussion, even though the information available is incomplete, it is obvious that there has been great difficulty in reducing the main items of expenditure. Armaments and debt service have been substantially maintained. Little new information is available concerning expenditure on social services. It is known that the scales of expenditure have been reduced in many countries, but the totals remain high. In almost every country there has been a considerable pressure to reduce ordinary administrative expenses. Civil service salaries have been reduced, in many cases more than once, the services have been re-organised

and reduced, and economies have been made which amount in the aggregate to large sums.

Perhaps the most considerable economies have been made, however, in investment expenditure and in public works. While such economies are not general and, in particular, are definitely challenged in a few countries which have deliberately embarked upon policies of expansion based upon borrowed money, they have formed a large part of the savings made in public expenditure in most countries. Thus, in the United Kingdom it has been estimated that the capital expenditure by the Government and local authorities on public works fell between 1929-30 and 1932-33 by 35 per cent. ¹ Expenditure on housing, roads and school buildings fell substantially, and only expenditure on electrification steadily increased.

Many other examples could be given of severe economies in capital expenditure during the depression. In Australia, for instance, where the building of roads, railways and bridges depends largely upon borrowed capital, and equally in many European and Latin-American borrowing countries, the reductions were very heavy. Thus, in Australia, the Commonwealth loan expenditures for works fell from £8.7 million in 1927-28 to £2 million in 1930-31, and in the Australian States from £35.6 million to £12.7 million. ² In Italy, the expenditure on public works fell from 2,048 million lire in 1928-29 to an estimate of 1726 millions in 1931-32. ³

Those countries which pursued contractionist policies also reduced this item of their expenditure very drastically. In the Netherlands, in 1931, 66 million gulden were invested in public works and transport ; in 1933, only 35 million gulden. ⁴

On the other hand, there were several countries which, in the later stages of the depression, deliberately embarked upon policies of increased capital expenditure on public works as a remedy for unemployment. The most definite example is that of Sweden. For the financial year 1933-34, budget provision was made for an increase of capital expenditure from 116 to 243 million krona, of which 160 millions is devoted to new public works, and a deficit was forecast of 242 million krona, to be covered chiefly by the flotation of new loans. In order to facilitate a comparison of the figures involved in this new public works programme, the main budget items of recent years have been tabulated.

¹ Royal Institute of International Affairs, "Monetary Policy and the Depression", Oxford University Press, 1933, page 92.

² Commonwealth of Australia Official Year-Book, 1932.

³ *Boletino Mensili de Statistica*.

⁴ Rotterdamsche Bankwerveeniging, *Monthly Bulletin*, 1933.

Swedish Government Expenditure 1928-29, to 1933-34. 1
Budget estimates, krona (000,000's).

	Closed accounts				Voted estimates	Draft estimates
	1928-29	1929-30	1930-31	1931-32	1932-33	1933-34
Effective expenditure	701.2	702.1	733.7	765.8	772.5	738.2
Repayment of debt . . .	24.6	40.9	31.9	38.6	8.0	47.5
Total	725.8	743.0	765.6	804.4	780.5	785.7
Revenue receipts	732.4	778.5	782.9	736.5	765.8	787.6
Balance	+ 6.6	+ 35.5	+ 17.3	- 67.9	- 14.7	+ 1.9
Capital outlay	65.8	68.1	52.9	89.5	115.6	243.4
Balance	- 59.2	- 32.6	- 35.6	- 157.4	- 130.3	- 241.5
Covered by proceeds of loans	46.2	22.2	41.9	68.2	97.2	236.6
Covered by Treasury balances	13.0	10.4	—	89.2	33.1	4.9

A special feature of this Swedish experiment needs to be mentioned. It is realised that borrowing for expansion of public works involves governmental as distinct from private provision of capital equipment. The loans proposed, therefore, are to be repaid within four years, mainly by the imposition of heavy new increments to the death duties.

The first instalment of borrowing for this purpose was a loan of 50 million krona and any amount subscribed in excess of this figure, offered for public subscription in April 1933. The terms of the loan were 4 per cent interest, issued at 97 and redeemable between 1934 and 1938; but these terms were not regarded as sufficiently attractive, and only 30,900,000 krona were subscribed.

Finland, also, has planned an expenditure in 1933-34 of 350 million marks to be obtained by borrowing and used for public works.² Czechoslovakia plans also to float a big loan at 5 per cent in order to carry out a programme of capital construction for the relief of unemployment. The subscription to that loan amounted to 2,000 million koruna.

The largest experiments in this direction, however, are apparently to be taken by the United States Government. In the early stages of the depression, public works were maintained

¹ "Bilaga til Statsverkspropositionen för 1933-37"; cf. G. MYRDAL: "P. M. Angående verkningarna på den ekonomiska konjunkturutvecklingen i Sverige av olika åtgärder inom den offentliga hushållningens område, Bilaga III, till Statsverkspropositionen för 1933-34".

² *Bank of Finland Monthly Bulletin*, December 1932.

on a large scale, but a contractionist policy was later followed. Immediately upon taking office, however, the new Government launched a programme of legislation involving various schemes for the promotion of trade recovery and unemployment relief. The most important of these measures was the introduction of the National Industrial Recovery Act, which came before Congress on May 17th and combined a comprehensive project of industrial regulation with a \$3,300 million public works plan. The Act is divided into two main parts; the first has for specific purpose "the encouragement of national industrial recovery and the fostering of fair competition". Part II concerns public works projects to be undertaken either by the Federal Government or by States and municipalities. Except in the case of highway construction, for which \$400 million is allotted, grants to local authorities must not exceed 30 per cent of the cost. To finance the programme, bonds are to be issued to the maximum amount of \$3,300 million, and provision is to be made for a sinking fund of 2½ per cent of the amount issued. Clauses were inserted by the House of Representatives calling for an increase of income-tax receipts, an extension of taxes to corporate dividends and a Federal petrol tax. The powers conferred by the Act are limited to a period of two years.

In the United States, it is noticeable that this expansion of the investment expenditure has been accompanied by considerable reductions of other expenditure. Reductions in the latter are expected to save \$1,000 million or more a year.

BALANCING THE BUDGETS.

Popular interest in the financial position of central Governments is usually centred in their general budgets and accounts, and the deficits which are the subject of parliamentary and Press discussion as a rule relate only to the deficits of those budgets and accounts. On the other hand, the meaning of those deficits is different in the various countries. To begin with, the deficits under discussion are not always cash deficits and do not, therefore, constitute an immediate drain on the existing Treasury balances, but in some cases represent differences between claims and liabilities or even commitments which will to some extent affect the Treasury balances of future years. Further, they may mean, in some cases, the failure of tax and other revenue proper to meet the requirements of the administrations which are included in the general budget. In other cases, they may mean the demand on the Treasury after provision has been made by realisation of State assets or even by raising funded

loans. On the other hand, the requirements of the administrations include expenditure on repayment of debt, or on advances or loans granted — expenditure which has an influence on the financial balance as a whole. In some case they include amounts which are in reality surpluses to cover deficits of previous years.

The budgets and accounts, therefore, need careful and minute analysis before the true financial position in either its narrower (cash deficit) or its broader (financial deficit) sense with regard to the general budget can be established.¹ The table on page 183 shows, for a number of countries, the balances of the budgetary accounts as indicated in the official documents, but after deduction of proceeds of loans and utilisation of Treasury cash balances.

These figures may be supplemented by the fuller information given in the *Statistical Year-Book*, 1932-33, and should be read with the detailed notes given there.

Such calculations, however, are far from disclosing the whole financial situation of any particular Government. The existence of many other accounts than those usually included in budgetary statements of revenue and expenditure renders necessary a much more extended investigation in each particular case. Such investigations, comprehending not only the general budget accounts but also special accounts — such as for autonomous State undertakings like railways, the deficits in respect of which are in some cases directly covered by the Treasury; or special accounts of amortisation funds and other capital expenditure, such as that on public works or, especially in recent times, on financing vast schemes for relief of distress in various economic branches in the different countries — demand for any country an extensive analysis of data scattered over a great number of different documents. In previous editions of the *Statistical Year-Book*, and in the *Survey* for 1931-1932, such calculations have been made in an attempt to estimate the total result of the year's financial transactions upon the financial situation as a whole. The final figures which appear in such calculations, however, are so different from those usually published as to lead to misunderstanding which it requires a great deal of explanation to avoid. They are, in any case, not available this year, and therefore it should be emphasised again that the table given below, while based entirely upon official information, should not be taken as representing the net financial situation of the public accounts of any of the countries cited.

¹ It is interesting in this connection to note that certain countries (*e.g.*, Denmark) are endeavouring so to organise their budgets that the results may show the economic position (increase or decrease of the net property of the State) rather than the financial position only.

*Surplus or Deficits of Budgetary Accounts, including
Amortisation Payments,¹
(Closed accounts.)*

Country	Financial year	Surplus or deficit	
		National currency (000,000's)	As a percentage of receipts
Austria	1929	+ 20	+ 1
	1930	— 262	— 13
	1931	— 322	— 16
Czechoslovakia	1929	+ 169	+ 2
	1930	— 275	— 3
	1931	— 3,128	— 34
Germany	1929-30	— 712	— 7
	1930-31	— 1,085	— 10
	1931-32	— 602	— 7
Greece ²	1929-30	+ 143	+ 1
	1930-31	— 9,626	— 91
	1931-32	— 1,453	— 15
	1932-33	— 4,224	— 51
Italy	1929-30	— 1,532	— 8
	1930-31	— 4,469	— 22
	1931-32	— 4,586	— 23
Japan	1929-30	— 200	— 13
	1930-31	— 189	— 13
Netherlands	1929	— 47	— 5
	1930	— 44	— 5
	1931	— 146	— 21
New Zealand	1929-30	— 1.6	— 8
	1930-31	— 3.6	— 17
Poland	1929-30	+ 37	+ 1
	1930-31	— 64	— 2
	1931-32	— 206	— 9
Sweden	1929-30	— 29(29.3)	— 4 (3.7)
	1930-31	— 33(32.5)	— 4 (4.1)
	1931-32	— 116	— 15
Switzerland	1930	+ 6.7	+ 2
	1931	+ 2.3	+ 1
United Kingdom	1929-30	— 25	— 3
	1930-31	— 23	— 3
	1931-32	— 8	— 1
United States	1929-30	+ 180	+ 4
	1930-31	— 853	— 26
	1931-32	— 2,885	— 136
U.S.S.R.	1928-29	— 568	— 8
	1929-30	— 643	— 6
	1930-31	— 3,043	— 15

For footnotes see following page.

The growing deficits have to be met, and one way is the realisation of existing State assets. The other is the raising of loans. The realisation of State assets, excepting Treasury assets proper, is, however, in most cases included in the receipts before any deficit representing a demand on the Treasury becomes apparent. The realisation of Treasury assets, without at the same time having recourse to borrowing, is necessarily limited lest the Treasury should be deprived of indispensable working funds. A few examples will illustrate these facts.

After deducting the proceeds of loans from the deficits, as shown in the preceding table, the balance representing the demand on the Italian Treasury was 1,142.9 million lire for 1929-30 and 463.3 million lire for 1931-32; whereas, in 1930-31, the proceeds from loans not only covered the budgetary deficit, but brought 365.2 million lire to the Treasury, so that the net deterioration of the Treasury position at the end of the three years was 1,241 million lire. This deterioration was represented by an increase in the Treasury liabilities (floating debt, current accounts, etc.) from 5,558.1 million lire to 9,374.1 million lire (i.e., by 3,816 millions), against which there was an increase of the Treasury assets from 1,062.1 to 3,637.1 millions — i.e., by 2,575 million lire. There was, in other words, a net increase of the Treasury liabilities by 1,241 million lire.

The Swedish deficit accumulated during the last three years amounted to 178 million krona, of which 132 millions were covered by loans, leaving a final demand on the Treasury of 45.6 million krona, which resulted in a diminution of the cash balance from 166 to 120.4 million krona.

In Greece, the accumulated deficit of the last four years amounted to 15,159.8 million drachmæ, of which 12,915.7 millions were covered from loans, leaving a demand on the Treasury of 2,244.1 million drachmæ. The balance between Treasury assets and liabilities, which stood on March 31st, 1933, at 4,027.8 million drachmæ to the favour of the Treasury, was thus reduced to 1,783.7 million drachmæ, and the cash in hand from 532 to about 160 million drachmæ.

Another indication, though not an exact measurement, of

Notes to table on previous page.

¹ Cash amortisation expenditure included; loan receipts excluded. For further explanation, see table in the section on "The Adjustment of Public Expenditures" in this chapter.

² The above results represent receipts and disbursements during the twelve months of a financial year without consideration as to whether they belong to the current budget or to the preceding budgets, to the budgetary accounts proper or to the arrears accounts (see Table 5b of the Financial Committee's report on the Financial Situation of Greece (document C.387.M.194.1933.II.A)).

changes in the financial situation may be obtained from the statistics which show the growth of public debt. There is a fairly general tendency for debt to increase, and this obviously indicates that deficits, after deducting the portion which is due to repayment of debt, are being covered by fresh borrowings.

The totals of debt shown in the table on the following page indicate, as a rule, the nominal amount of capital outstanding. This, however is sometimes difficult to calculate, particularly when the debt service is in the form of annuities which do not distinguish between interest and amortisation. In some cases, the figures, as indicated in the official statements, indicate the gross indebtedness, and, in other cases, the net indebtedness after deduction of sinking funds and securities withdrawn but not yet cancelled. As in the preceding table, the statistics are not comparable internationally and are given merely to indicate the general trend of development. They cannot be used to indicate the financial situation of any particular country except after careful examination of their exact meaning as disclosed by more detailed information.

Examination of this table, however, shows that the total amount of the public debt (excluding the debt of regional and local authorities) increased during the depression in all the countries cited except France, where there was a substantial decrease in the debts owed abroad, offset in some degree by an increase in the floating domestic debt. The major part of this decrease took place in the financial year 1931-32, when the French Government continued its policy of buying French bonds issued abroad.

The increase of total public debt in this period was small in the United Kingdom and also in Australia, India and New Zealand.

More complete information is available, covering fifty-seven countries, in the *Statistical Year-Book* of the League of Nations for 1932-33.¹ The statistics there given divide the debts of each country into foreign and domestic debt and the latter into funded and floating debt.¹ The most cursory examination of these statistics will indicate the multiplicity of forces at work. For example, many of the weaker financial countries have found it impossible to contract new long-term loans in foreign markets, and very difficult to raise domestic long-term loans, but have increased their floating indebtedness both on foreign and on domestic account.

¹ Table 111.

*Public Debt in Certain Countries, 1929 to 1933, at the End of the Financial Year.*¹

National currencies (000,000's).

Country	Currency	Month in which the financial year ends	1929	1930	1931	1932	1933
Argentina :		XII					
Total	Peso		3,050	3,374	3,634	...	...
External			1,071	1,210	1,066	...	...
Australia :		VI					
Total	£A		1,104	1,101	1,156	1,188	...
External			572	574	599	602	...
Austria :		XII					
Total	Sch.		1,866	2,229	2,262	2,991	...
External . . . . .			..	2,092	2,031	2,226	...
Belgium :		XII					
Total	Franc		52,305	52,742	52,629	...	...
External			27,668	26,766	25,629	...	...
Canada :		III					
Total	¢C		2,647	2,545	2,610	2,832	...
External			481	423	519	491	...
Chile :		XII					
Total	Peso		2,688	3,242	3,310	3,869	...
External			2,289	2,483	2,431	2,827	...
France :		III					
Total	Franc		468,512	482,179	480,821	459,746	...
External			179,847	202,306	197,781	175,430	...
Germany :		III					
Total	RM.		8,972	10,375	12,089	12,137	12,247
External			901	854	3,306	2,215	3,065
India :		III					
Total	Rupee		10,745	11,365	11,604	12,150	...
External			4,718	4,882	5,170	5,079	...
Italy :		VI					
Total	Lira		88,942	89,876	93,178	97,268	98,418
External			1,808	1,774	1,736	1,696	1,653
Japan :		III					
Total	Yen		5,831	5,959	5,956	6,187	6,741
External			1,451	1,447	1,479	1,473	1,391
Netherlands :		XII					
Total	Gulden		2,727	2,681	2,877	...	...
External			—	—	—	—	—
New Zealand :		III					
Total	£NZ		264	267	276	282	...
External			154	151	159	...	...
Poland :		VI					
Total	Zloty		4,079	4,079	4,428	5,041	5,054
External			3,799	3,694	3,988	4,593	4,514
Sweden :		VI					
Total	Krona		1,835	1,801	1,846	1,795	...
External			—	—	—	—	—
United Kingdom :		III					
Total	£		7,621	7,596	7,583	7,648	...
External			1,085	1,074	1,067	1,091	...
United States:		VI					
Total	\$		16,931	16,185	16,802	19,487	21,426
External			—	—	—	—	—
Union of S. Africa :		III					
Total	£SA		244	250	257	264	...
External			151	156	161	160	...

¹ Book value without regard to foreign exchange fluctuations.

The figures given above for total indebtedness, therefore, include several different kinds of debt. Strong financial countries with good credit may cover budget deficits and raise money for capital expenditure or special purposes by floating long-term loans. In recent years, the possibility of floating such loans on foreign markets has practically vanished; but domestic loans have been floated by countries whose citizens retain confidence in their Government's credit and have reserves.

Short-term loans such as those obtained by the issue of Treasury bills may also be used, and there is evidence that this method has been considerably extended both in countries where such bills have long been familiar and by the creation of a bill market in countries like Australia.

Weaker financial countries with limited possibilities of borrowing may have to resort to advances from their Central Banks. An examination of the Central Bank loans to Governments will, however, show that considerably increased borrowing from Central Banks up to the end of 1932 has been the exception rather than the rule.

Countries which have incurred extraordinary expenditure on frontier disputes are among those which have most increased their indebtedness to the Central Banks. In Peru, where the Government at the end of 1931 had no Central Bank debt, this item amounted to about 180 per cent of the note circulation at the end of 1932. In Bolivia, the obligations of central and local Governments amounted in 1929 to about 10 per cent of the note circulation, and by the end of 1932 was about 190 per cent. The Japanese Government's debt to the Bank of Japan amounted, in 1930, to only about 15 per cent of the note circulation, but at the end of 1932 this had risen to 45 per cent.

Exceptionally important increases also took place in Russia, where the Government debt to the State Bank in 1928 was less than 15 per cent, but has since increased to about 75 per cent at the end of 1931; and in Chile where the amount was 3 per cent of the note circulation in 1928 and 135 per cent at the end of 1932.

In most other countries the budgetary position has not yet led to any pressure on the Central Banks, and some Governments have even been able to reduce their obligations to these institutions.

The course of the budgetary deficits may at first sight appear to have much in common with the events which led to the currency difficulties in the years immediately after the war, but it should be emphasised that public finance is not, in this depression, such a dominating factor in the creation of currency disorder as it was then.

On the other hand, this analysis has stressed the fact that

the balancing of the budgets is a problem of increasing importance and difficulty, as Treasury reserves and taxation capacity become exhausted and borrowing possibilities diminish.

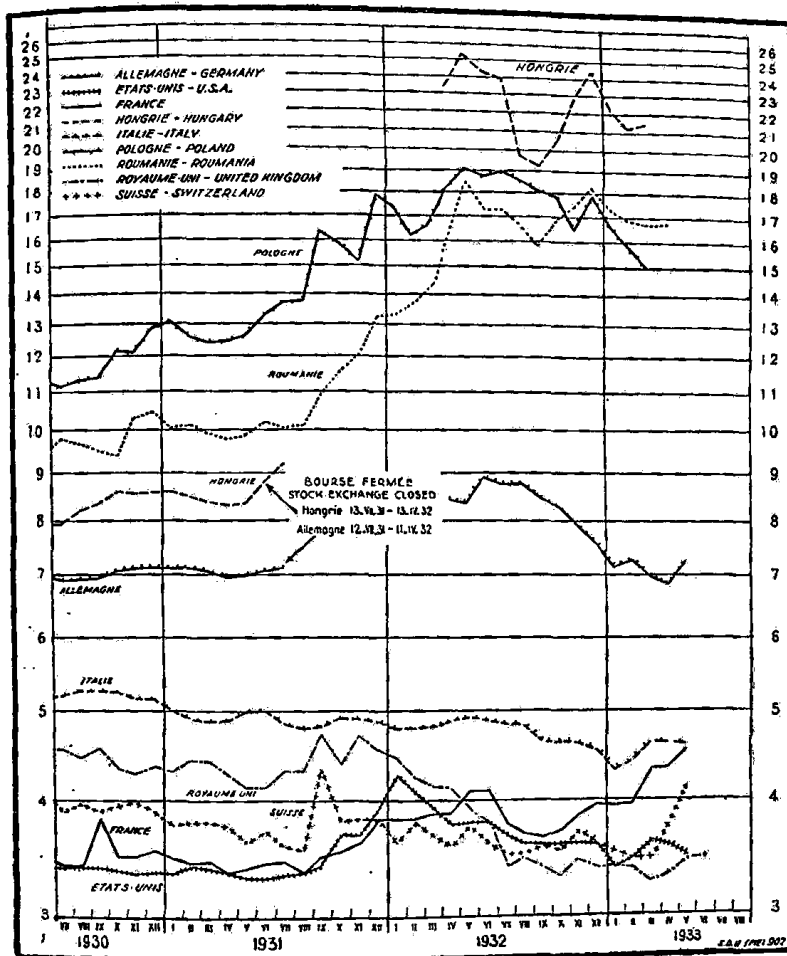
In the countries whose reserves of taxable capacity had been largely exhausted by economic difficulties extending over many years, borrowing capacity was low also, and the depression has therefore driven them to very drastic controls of expenditure in order that the resources of their Central Banks might not be overstrained by advances to the Government Treasury. The plight of these weaker countries illustrates the sequence of events by which the public finances of a country become a source of economic danger in a long-continued depression. The inflexibility of expenditure causes first a search for additional revenue and then resort to the loan market. If the budget cannot be balanced before taxable and borrowing capacity show signs of exhaustion, the Government is forced to get advances directly from the Central Bank. Once this position is reached, care has to be taken lest the Central Bank's reserves be so weakened as to induce distrust of the national currency. If such distrust becomes widespread and there is a flight from the currency, either externally by the purchase of foreign exchange or internally by the purchase of goods, monetary inflation is a real danger. The bank's reserves against credit withdrawals need to be protected either by issuing inconvertible money or by limiting the right of withdrawing deposits. Only the firmest control both of the banking and of the budgetary situation can check inflation once this stage is reached.

This sequence of events has been set out rather as an indication of the important consequences that hang upon the achievement or maintenance of budgetary stability than as a description of what has happened or is likely to happen. Such a sequence, varied as it may be in individual cases, is well known after the experience of the post-war inflations, and those countries which have already suffered in this way are likely to strain every nerve to prevent a repetition of the experience.

The diagrams which follow continue, for the year 1932 and the first months of 1933, the similar diagrams reproduced in the *Survey* for 1931-32. They show the price of long-term capital which Governments have to pay in national markets and in the London capital market. It is striking to note the considerable improvement which has taken place during the last year, and especially for those countries which have access to the London capital market. In order to appreciate this improvement, it may also be of interest to notice the activity of the different bond markets given in the table below. The increased number of sales will undoubtedly facilitate new issues.

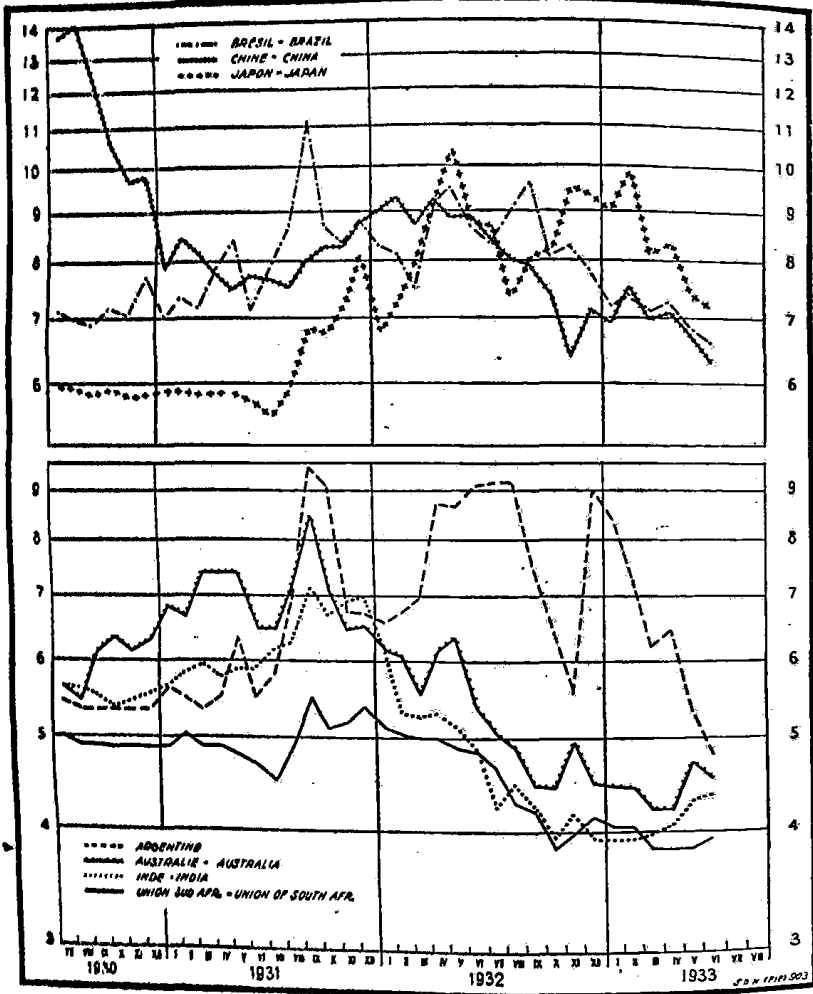
Actual Percentage Yield of Certain Bonds or Groups of Bonds.

A. According to Domestic Quotations.¹



¹ France : Rentes perpétuelles 3%.
 Germany : Miscellaneous bonds, 8% and less.
 Hungary : Forced Loan 1924, 5%.
 Italy : Rentes, 3 1/2%.
 Poland : Miscellaneous Government bonds.
 Roumania : Government bonds.
 Switzerland : Railway bonds.
 United Kingdom : Consols, 2 1/2%.
 United States of America : Treasury bonds.

Actual Percentage Yield of Certain Bonds, or Groups of Bonds.
 B. According to London Quotations. ¹



¹ Brazil : 5% Funding, 1914.
 China : 5% 1913 Re-organisation Loan.
 Japan : 6% 1924.
 Argentina : 4% Recission.
 Australia : 5% Registered.
 India : 3 1/4% Government stocks.
 Union of South Africa : 5% Inscribed.

Stock Exchange Turnover of Bonds, 1932-33.¹

Country	Bonds	Unit of turnover	1932								
			I	II	III	IV	V	VI	VII	VIII	IX
Argentina . . .	Central Government Provincial and municipal	\$ (000,000's)	23.2	18.3	21.3	27.0	21.3	21.4	20.5	20.5	24.8
			5.0	2.4	3.5	6.2	4.3	4.7	3.6	4.2	3.6
Czechoslovakia	All	Number of sales (000's omitted)	14.7	13.3	8.7	9.8	9.1	9.5	7.1	15.6	25.0
France	Oblig. and rents	Quantity sold 1931=100	67	63	64	65	119	102	138	105	336
Germany . . .	Gross sale of German bonds	RM. (000,000's)	39	24	17	25	21	19	31	25	37
Italy	All	Lire (000,000's)	3.4	6.5	4.3	3.8	3.0	2.0	4.2	2.5	15.0
Sweden	All	Krone (millions a day)	1.6	1.5	1.5	0.7	0.5	0.5	0.6	0.7	0.7
United Kingdom	Government and municipal loans	£ (000,000's)	29.2	29.0	37.2	33.5	37.1	38.1	56.7	35.7	38.5
United States	Liberty and Treasury (a) All	\$ (000,000's) (par value)	67.7	54.7	51.3	68.9	86.8	67.0	46.4	25.8	24.4
			292.9	222.5	252.7	254.2	261.6	255.8	243.6	344.5	246.2

¹ Argentina : *Banco de la Nacion, Economic Review.*
 Czechoslovakia : *National Bank Bulletin.*
 France : *Statistique générale de la France, Supplément mensuel du Bulletin trimestriel.*
 Germany : *Deutsche Volkswirt.*
 Italy : *La Vita Economica, Baramestro Economica.*
 Sweden : *Kommersiella Meddelanden.*
 United Kingdom : *Economist.*
 United States : *A Survey of Current Business ; (a) Standard statistics.*

*Stock Exchange Turnover of Bonds, 1932-33*¹ (continued).

Country	Bonds	Unit of turnover	1932			1933					
			X	XI	XII	I	II	III	IV	V	VI
Argentina . . .	Central Government	\$ (000,000's)	21.7	21.9	26.4	25.2	24.3	34.8	31.7	47.5	...
			2.8	2.6	3.4	2.4	2.4	4.0	2.8	3.9	...
Czechoslovakia	Provincial and municipality	Number of sales (000's omitted)	21.4	9.1	10.2	10.4	9.2	8.7	17.8	22.0	...
			132	85	77	64	77	134	83	93	101
France	Oblig. and rentes	Quantity sold 1931=100	132	85	77	64	77	134	83	93	101
Germany . . .	Gross sale of German bonds	RM. (000,000's)	28	26	36	166	69	110	30	22	app.18
			12.2	6.2	9.9	31.7	13.7	16.8	10.1	10.7	18.3
Italy	All	Lire (000,000's)	0.7	0.7	0.6	0.7	0.7	0.6	0.7	0.9	0.8
Sweden	All	Krone (millions a day)	0.7	0.7	0.6	0.7	0.7	0.6	0.7	0.9	0.8
United Kingdom	Government and municipal loans	£ (000,000's)	44.2	38.5	32.7	37.2	35.2	39.4	29.2	37.5	36.6
United States	Liberty and Treasury (a)	\$ (000,000's) (par value)	20.3	15.8	37.4	38.4	45.4	55.2	61.0	38.4	—
			189.3	159.4	249.2	263.0	231.5	192.1	271.3	374.0	377.7

¹ For note, see preceding page.

Chapter VII.

INTERNATIONAL TRADE AND COMMERCIAL POLICY.

THE TARIFF WAR.

In a previous volume, the story of increasing trade restrictions was carried up to the early part of 1932.¹ The period of tariff warfare which was renewed after a temporary lull at the time of the World Economic Conference in 1927 culminated in the United States tariff of 1930, and the new British tariff of 1931-32; but these events were merely the outstanding examples of a widespread tendency. It is, indeed, difficult to summarise with accuracy the many tariff increases that have recently been imposed, to say nothing of the emergency trade restrictions which are the subject of the following section. The Hawley-Smoot tariff in the United States was the signal for an outburst of tariff-making activity in other countries, partly at least by way of reprisals. Extensive increases in duties were made almost immediately by Canada, Cuba, Mexico, France, Italy, Spain. During 1931, general tariff increases were announced by India, Peru, Argentine, Brazil, China, Italy, Lithuania. In addition, there were increases of duties upon individual items or groups of commodities in most of the countries for which information is available, often on several occasions. When currency instability on a wide scale was unloosed after the United Kingdom abandoned the gold standard in September 1931, tariff increases, like other restrictions on trade, began to follow one another in the most rapid succession. During 1932, there were general tariff increases in the United Kingdom, Egypt, Norway, Japan, Portugal, Greece, Siam, South Africa, Australia,² Belgium, Latvia, the Netherlands, the Dutch East Indies, Nicaragua, Persia and Venezuela. Partial

¹ *World Economic Survey*, 1931-32, Chapter X.

² On February 25th, 1932, there was a downward reduction of the Australian tariff, followed on October 14th, in accordance with the Ottawa agreements, by an upward revision on about 400 items imported from foreign countries.

increases, repeated several times in most cases, were recorded in practically every country for which information is available. There were some downward adjustments of particular items, but the general trend towards increase was very clear. There was probably never any period when trade was subject to such widespread and frequent alterations of tariff barriers. The tariff warfare naturally fed on itself and has continued to do so as duties have been de-consolidated, treaties have been denounced or allowed to expire, currency instability has led into a maze of new protectionist regulations and private trading initiative generally has given way to administrative controls.

During the first months of 1933, the process continued. Sweden, Norway, Czechoslovakia, Poland, Switzerland, Hungary and the United Kingdom were among the countries which raised their tariffs in whole or in part during the first three months of the year. Germany, having freed herself from certain consolidations of duties established in the Franco-German commercial agreement of 1927, introduced further measures of agricultural protection, and France, in order to restore her trade balance with Germany, at once imposed further quotas on certain German imports. France also took steps to counteract the effects of currency depreciation upon exports from the United Kingdom, from several British dominions and colonies, and Japan. Several British dominions and colonies revised their tariffs in accordance with the Ottawa agreements, reducing some duties on British goods but increasing a larger number upon foreign goods. In the United States the House of Representatives in February rejected a bill to increase the duties on goods from countries with depreciated currencies, but certain duties were raised under the flexible provisions of the tariff.

No mere recital of countries where changes have been made is adequate to convey a full impression of the variety and importance of the new trade barriers that have been erected. Unfortunately, no recent statistical calculations are available to measure the relative effectiveness of different tariffs, and, in any case their usefulness would be diminished at the present time when, in addition to tariffs, quotas and a host of other restrictions interfere with the free flow of trade. An even more serious obstacle to trade than the actual height of tariff rates is the uncertainty to which the continual changes give rise. Treaties which gave some assurance of stable conditions over a period of years have in most cases been replaced by temporary agreements for a few months at a time. Prudent investors are naturally reluctant to risk their capital in enterprises dependent upon foreign trade when there is so little certainty about the conditions upon which that trade may be conducted.

Moreover, when trading agreements and regulations are

in such a fluid state, the temptation to manoeuvre for bargaining positions in view of possible negotiations for tariff reductions becomes almost irresistible. The method by which a nation seeks to equip itself for bargaining by imposing, or threatening to impose, higher tariffs which it is, in fact, prepared to abandon by way of apparent concessions is apt in such circumstances to degenerate into a general scramble for tariff increases.

On the other hand, reference should be made to three important recent developments in the field of commercial policy. The first, already noted in last year's *Survey*,¹ is the agreement negotiated by Belgium, the Netherlands and Luxemburg for the general and progressive lowering of their tariffs over a series of years. This agreement, negotiated at Ouchy at the time of the Lausanne Conference and signed at Geneva on February 20th, 1933, is supplemented by two other agreements concerning foreign residence and labour, and concerning fiscal co-operation for the avoidance of double taxation.² All three are framed in the spirit of the principles of international economic co-operation worked out in the course of discussions by the League's Committees, and therefore offer a model for the negotiation of wider agreements. Up till the end of April, however, no other country had taken advantage of this Dutch-Belgian initiative.

The second is to be found in the Ottawa agreements between the constituent members of the British Commonwealth and the British Empire. It is essential to separate clearly the fact that the United Kingdom, after December 1931, became a protectionist country from the negotiations subsequently initiated at Ottawa in July 1932. The imposition by the United Kingdom of substantial tariff duties on a wide range of imports, obviously narrowed in a very important degree the freedom of world trade. The effect of that action, and of the subsequent policy of agricultural re-organisation behind the shelter of quotas, has been all the greater because of Britain's traditional adherence to free trade principles for the greater part of a century. But the actual agreements negotiated at Ottawa upon the basis of the new regime may somewhat counterbalance the restrictions on trade. Under the agreements the Dominions undertake to set up Tariff Boards which will duly consider representations from the exporters in the other British countries concerned, thus conceding the principle of mutual negotiation on tariff policy. In many of the Dominions, notably in Canada and Australia, and the

¹ Pages 308-9.

² "Traité de Commerce entre le Royaume des Pays-Bas et l'Union économique belgo-luxembourgeoise"; "Convention d'établissement et de travail entre les Pays-Bas et la Belgique"; "Convention entre les Pays-Bas et la Belgique pour éviter les doubles impositions et régler certaines autres questions en matière fiscale".

Colonies, concessions were made with the object of stimulating inter-Imperial trade. These concessions were accompanied in practically every case by some raising of the barriers against foreign goods, and it is not possible yet to judge from the statistics of a limited period, during which the crisis has been aggravated, as to the net effect on world trade as a whole. In so far as the aggravation of the crisis was partly due to the closing of British markets against foreign goods and to the retaliations thereby provoked, it is probable that the net effect to date has been restrictive. On the other hand, it has been the declared policy of the Government of the United Kingdom to negotiate new treaties with its principal foreign customers starting from the basis of the new Imperial agreements. New treaties were concluded in May with Denmark and the Argentine, a more limited agreement was signed almost at the same time with Germany, and at the moment of writing negotiations are in progress with Japan, Norway and Sweden. The conclusion of these and similar negotiations was recognised as one of the exceptions made by various Governments to the tariff truce arranged as a prelude to the Monetary and Economic Conference.

The treaties already concluded are discussed later in connection with recent bilateral agreements. They are significant of the marked tendency at present towards regulated trade and consist, not only of agreements concerning the duties to be imposed, but of provisions which take into account the new quantitative regulation of trade by means of quotas, and even "take note of" agreements between trade organisations in the respective countries which form an integral part of the bargain struck. Thus, the United Kingdom, which a century ago led the way to free trade on a competitive basis, has now crystallised the modern trend to regulated or planned trade.

The third important development of commercial policy has resulted from the initiative taken by the Roosevelt administration in announcing its desire to lead the way to a worldwide reduction in tariffs. This initiative has been chiefly responsible for the plan of a tariff truce as a prelude to the Monetary and Economic Conference, a truce already agreed to with certain reservations by the main industrial countries.

THE IMPOSITION OF EMERGENCY TRADE RESTRICTIONS.

While the tariff war continued unabated during 1931 and 1932, another disconcerting element, new at least in its scope, was interjected into the situation by the rapid adoption in a large number of countries of emergency measures of trade restriction

aimed primarily at direct quantitative limitation of imports, and in some cases of exports. This new protectionism has not taken the place of higher tariffs — import duties, as was shown in the preceding section, are now higher and more flexible than ever. But it has effectively supplemented and completed their restrictive effects. Administrative measures, such as prohibitions, quotas, licensing systems and clearing agreements, have never before been used as a general method of trade regulation except in the altogether abnormal circumstances of the war and immediate post-war years. Particular commodities have been so regulated at certain times, but the wholesale application of administrative controls is new. Moreover, the background of the war and post-war regulations was essentially different from the present circumstances. Instead of there being a world shortage of commodities with a strong upward pressure of prices and widespread inflationary tendencies, the recent restrictions have been imposed at a time when there are heavy accumulations of stocks, very low and falling prices and worldwide deflation. The purposes — and economic background — of the new protectionism in 1931 and 1932 are so essentially different, therefore, that the experience of the past offers little help in analysing their effects and probable development.

In the present section, an attempt is made to distinguish and describe the various forms of trade regulation which have been established, to trace the course of their evolution in the last two years, to weigh their relative importance in restricting world trade and to indicate summarily the main consequences of their application which are already apparent.

It is important in such an analysis to bear clearly in mind the circumstances out of which the new protection arose. The dominant factor in the economic situation up till the last quarter of 1931 was undoubtedly the continued fall in prices, particularly of agricultural raw materials. This fall in raw-material prices continued with few exceptions after the widespread abandonment of the gold standard in the last quarter of 1931; but its importance after that date was overshadowed by the currency instability which disturbed international price equilibria and became the major preoccupation of commercial policy. The two main causes for this preoccupation were anxiety on the part of many countries with relatively weak currencies concerning their external balances of payments and the determination of many more not to allow their industries and their agriculture to be sacrificed in an abnormal period of price cutting and exchange dumping.

The first and simplest device employed as a supplement to higher tariffs consists usually of a system by which imports are prohibited except under licence and therefore become

possible only after permission has previously been obtained from the administrative authorities. While in some cases such licensing has not gone far beyond the registering and surveillance of import tendencies, in the majority of countries it has been accompanied by, or has led to, measures of direct control and limitation of the quantities imported. The varieties of procedure by which this result has been achieved are many ; but in essence they derive from the principle of prohibiting imports either wholly or partially in the case of certain specified products. Quota or contingent systems are a variant of the method of prohibition, under which only a stated quantity of specified imports is permitted. There are many differences, even within the same country, in the methods by which quota systems are administered. The fixing of the quota, both in time and among the exporting countries and the particular importers in each country, the surveillance of the system by Government departments, by the associated importers, by a grouping of exporters or by various combinations of these methods, and the manner in which the quotas are varied from time to time have developed according to the particular circumstances of the trades in question.

A more generalised control of imports is maintained in a great number of countries in the form of foreign-exchange control. The Central Bank is given power to impound the foreign exchange derived from export receipts. In the majority of cases, provision is made whereby payments for exports must be deposited with the Central Bank, which is also given power to mobilise as far as possible exchange derived from other sources. Payment for imports is thereafter possible, theoretically, only by obtaining the requisite foreign currencies from the Central Bank, which is, therefore, able to control the external drain upon its reserves and maintain the external parity of the country's money. In practice, the effectiveness of such foreign-exchange controls varies a good deal with the economic circumstances of the particular countries. In some, the invisible items in the balance of payments are so important, and the powers of the Central Bank so limited, that "black" markets quickly develop in which the national currency exchanges at depreciated levels. While, however, the Central Banks are not always able to exercise a fully effective control over their exchange rates and therefore over the quantities of goods imported, the existence of such controls in so many countries has been a powerful factor in compressing the total quantities and values of imports and therefore of exports.

Such direct controls either over the quantities of goods imported or over the means of paying for them are supplemented by a variety of administrative devices which limit importation directly. Prominent among these are new types of sumptuary laws, of which the most important are milling or mixing regulations

stipulating that, in the processes of manufacture, certain proportions of domestic products must be combined with the imported goods. Devised at least partly as a means to protect the secondary manufacturing processes, such as flour-milling, these regulations offer an effective check also to the use of imported raw materials and therefore to the quantities imported. The raising of consular, import and other administrative fees, the increasing severity of legislation requiring marks of origin, the indirect effect of veterinary or similar health regulations, and, in general, the considerable growth of administrative protectionism, add their influence to other forms of restriction.

The combined effect of all this multiplication of regulations has been to change the basis of international trading in many countries from one of individual freedom tempered by tariff restrictions to one in which trade is prohibited except by special permission in certain cases. As the area of control widens and the regulations multiply, the trade that is permissible is not only continuously reduced in volume, but becomes more variable and uncertain. There is little inducement to extend trading enterprise and still less to invest capital in producing goods for foreign markets when the possibilities of utilising such enterprise and investment profitably not only diminish, but are incalculable.

Two by-products of this situation need to be emphasised. The first is an inevitable increase in civil service interference with private initiative. The whole basis of foreign, and indeed of all, trade is the freedom to buy what one wants when one wants it and in the most advantageous markets. The middlemen who organise trade under a system of free enterprise must always be governed in the last resort by the satisfaction of the ultimate consumer. Under a system of controlled trade, the influence of the consumers' desires necessarily becomes less effective. The organised domestic producers are able to present their interests more immediately and effectively than the unorganised inarticulate consumers, and, as the consumers' range of choice is constantly narrowed, there is a strong trend towards a managed economy.

This trend is strongly reinforced by the second consequence of controlled trade — the encouragement to, and even pressure upon, the traders and producers to organise themselves into trade associations through which the controls can be managed. The more strongly organised cartels both of the exporting and of the importing countries are able to secure the lion's share of whatever trade is permissible, and where such cartels do not exist they are in rapid process of formation. The independent producer, both foreign and national, tends to be squeezed out, and the consumer to have his interests, and particularly his liberty of choice between competing products, ignored.

Mention should be made finally of the very rapid increase during 1932 of the various forms of clearing or compensation agreements, both public and private. The latter, which are sometimes described as truck or barter agreements, are a strange phenomenon in the modern age, symptomatic of the extent to which the normal media of exchange have broken down. The difficulty of devising means of payment for trade conducted in the normal fashion by the use of credit has led to agreements, between State organisations or private enterprises, for the bartering of goods against goods. Thus, the Turkish Ministry of Economy and an Austrian tobacco company entered into an arrangement on November 17th, 1932, by which the company agreed to buy, up to the end of June 1933, Turkish tobacco to the value of twenty million French francs, payable in Austrian merchandise. The Swedish Government made a similar arrangement with Greece to import Greek tobacco to the value of \$400,000, 20 per cent of which sum was to be written off the Greek debts in Sweden, the remaining 80 per cent being paid for in Swedish goods. Other examples are the compensation agreement between Hungary and Czechoslovakia of December 22nd, 1932, by which 29,000 Hungarian pigs are to be exchanged for 20,000 wagons of Czechoslovak wood fuel, and Hungarian eggs and similar products to the value of one and a-half million crowns are to be paid for by facilities accorded to Hungarian tourists in the Czechoslovak thermal stations. Similar barter agreements might be cited between European and also between South and North American countries. For example, in August 1931, the Brazilian Government concluded an agreement with the Grain Stabilization Corporation and the Bush Terminal Company of New York for the exchange during eighteen months of 1,275,000 sacks of coffee against 25,000,000 bushels of wheat. In consequence of this agreement, Brazil prohibited the import of wheat flour for eighteen months.

Clearing agreements, designed to regulate bilateral trade with individual countries so as to decrease passive balances and bring imports and exports more closely into agreement, have multiplied rapidly in recent months. Such agreements differ from the compensation arrangements just described in not specifying, as a general rule, the barter of particular commodities, but allowing trade to be regulated within certain limits by the ordinary commercial channels. In practice, however, as the new British treaties indicate, there is a tendency for the systems to fuse into a more general form of regulated trade. There are many complications in these negotiations, chief of which arise from the concern of the creditor countries that a reasonable proportion of the exports from their debtors shall be allocated

to the liquidation of existing commercial debt. Thus, one of the earliest series of clearing agreements, negotiated by Switzerland, provided that, in the case of Hungary, one-third of the receipts from Hungarian exports to Switzerland were to be credited to debt repayment until certain outstanding debts were cleared off, and after that one-fourth of the exports were to serve a similar purpose; in the case of Austria, the proportion was also one-third. Both of these treaties have since been terminated; but the principle has been applied in other cases, notably a series recently negotiated between Germany and her creditors. The Anglo-Argentine agreement concluded in March 1933 also included provision whereby debts were to be liquidated, in this case by means of a new long-term loan.

There has been much criticism of the clearing arrangements mainly on the ground that, in regulating bilateral trade, they interfere greatly with the triangular trade, which has been important in the past, and reduce the value of world trade as a whole. The source of a country's imports is not necessarily the best market for its exports nor the source from which it draws capital. Attempts to bring imports and exports between particular countries into a closer balance disturb existing marketing arrangements and tend to reduce world trade. It has been shown in the *Review of World Trade* for 1932 that the effect of the various attempts to regulate bilateral balances is already important, and it is probable that their full effect has not yet been achieved. However, the negotiation of clearing agreements continues. In the first three months of 1933 alone, such agreements were concluded by Switzerland with Roumania and Yugoslavia; by France with Bulgaria, Yugoslavia and Hungary; by Italy with Roumania and Sweden, and by Germany with Roumania. ✓

It is evident that commercial policy, in this as in other respects, is in a transitional stage. The regulation of trade by means of tariffs which in general apply to all other countries in approximately the same way is being replaced by a more elaborate network of negotiated bilateral treaties, which include quotas and other forms of quantitative regulation, private commercial agreements and financial provisions. The world is moving towards a greater degree of planned or regulated trade. The possibilities of somewhat enlarged trade emerging, as such negotiated agreements bring order out of the existing chaos, have recently appeared to be more encouraging; but the difficulty of balancing conflicting industrial and financial interests in any negotiation is very great, and there is danger lest the interests of third parties should be neglected in separate bilateral bargains. In view of the existing situation, reversion to the simpler competitive forms of tariff negotiation is administratively and econ-

mically less possible than before the depression encouraged the rapid evolution of varied forms of trade regulation ; but the newer types of agreement, it is recognised, need to be considered in the setting of an international and not merely a national economic situation.

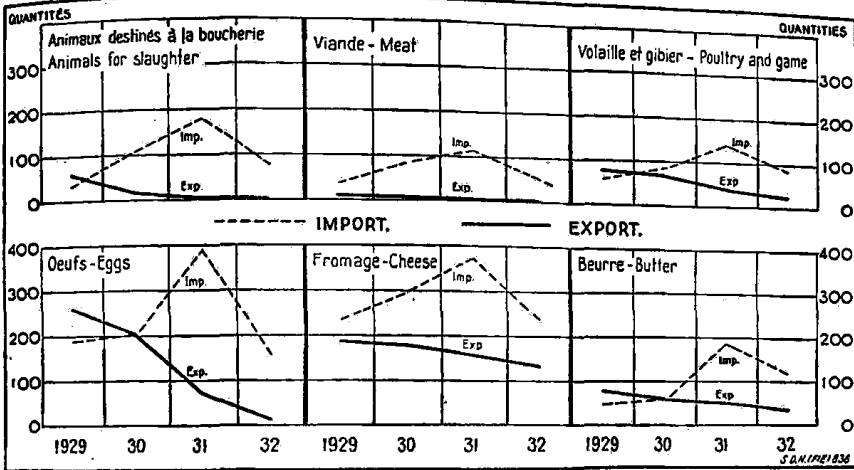
The extent to which quantitative restrictions of trade have been enforced has varied greatly from country to country. The restrictive effect of the measures enforced in different countries cannot, however, be accurately gauged. One country may apply restrictions to a very wide range of goods to a slight extent, another may rigidly control the imports of a limited number of commodities. France affords an example of a country in which the range of goods to which restrictive measures are applied is very large. In the early months of 1933, quotas had been applied to over 1,200 tariff items (about one-sixth of the whole), including many of the chief import groups. It has been estimated that more than one-third of the total value of imports is subject to quotas, and among the commodities affected are cereals, cattle and other farm products, fish, wine, fruits, wood fuel, semi-manufactured cotton and iron products, leather, hides, furniture, stockings, cotton tissues, papers, certain machines, glassware, etc. The import quota allowed varies from commodity to commodity and sometimes from quarter to quarter. There are commodities where the quota is no more than 50 per cent or less of the average quantities imported before the depression. Sometimes these quotas are fixed by the competent Ministry, in other cases the imports to be limited and the quantities permitted are established by agreements between the domestic and foreign producers, ratified by the Government. The restrictions are, at the moment of writing, still being extended to new commodities, a notable recent example being the temporary quotas imposed in 1933 upon about thirty classes of imports from Germany after the de-consolidation by Germany of certain agricultural duties established by the Franco-German agreement of 1927. The general effect of the quotas in checking the strong tendency for imports to increase is clearly shown in the diagram on the next page.

The particular example of France might, if space permitted, be supplemented by similar details concerning other countries. In Italy, for example, there is a quota system affecting imports from countries which impose quotas on Italian goods. In Holland, about one-tenth of the total imports are subject to quotas which, however, are ample in scope ; in Poland, prohibitions mitigated by licensing systems extend to about one-fourth of the total imports ; in Switzerland, an extensive quota system also covers about one-fourth of the imports.

France : Trade in Certain Animal Food Products, 1929-1932.

Animals for slaughter and meat are shown in thousand metric tons, and other products in hundred metric tons.

----- Imports. ——— Exports.



One of the most effective systems of exchange control is practised by Germany. From July 1931, when Germany was forced to demand a moratorium for her political debts, all transactions in foreign exchange have been controlled by the Reichsbank. Exporters are required to declare their exports to the bank, which has the right to demand that at least a part of the foreign currencies so acquired shall be remitted to it. Importers draw the necessary means of foreign payment from the bank in accordance with regulations made each month fixing the conditions under which importation is permitted. More or less similar exchange controls exist in a very large number of other countries, covering a substantial portion of the world's trade.

It is unnecessary to give further concrete examples of the actual working and scope of the various forms of quantitative import restrictions. The impression given by tabular statements recording the new measures taken in various countries from month to month is that the range and complexity of such restrictions have constantly increased since the middle of 1931.¹

¹ Cf. the tabular statements in *World Economic Survey*, 1931-32, pages 319-322, and in *Index*, Vol. VIII, No. 85, January 1933, pages 6-13, with Appendix I of this *Survey*.

Such an impression is supported by more detailed investigation of particular national cases. The frequency of change, the number of commodities affected, the limitations imposed, tend, with few and slight exceptions, to increase. There is, moreover, a strong tendency for such restrictions to perpetuate themselves and propagate others.

It remains to consider the principal ways in which the consequences of the new quantitative restrictions on imports differ from those of tariff increases.¹ In such a consideration it is, however, necessary to emphasise again the important fact that quantitative restrictions supplement but do not replace higher tariffs. In the decline of world trade recorded later in this chapter, it is impossible to separate the effects of the higher tariffs that are constantly being imposed from those of other trade restrictions. All that can be done is to record their combined effects.

But there are certain ways in which the application of quantitative restrictions differs from the imposition of tariffs. Now that tariff policy has become so fluid and commercial treaties are limited to such short periods, tariffs as well as quotas lead to greater uncertainty, which is in itself a restrictive influence. Quotas and similar quantitative controls are perhaps more changeable and give greater powers to administrative officials. But the chief difference between such controls and tariffs lies in the point at which they are applied. An increase in the import duty charged on a particular commodity tends to raise the price at a sensitive point in the wholesale bargaining process. The equilibrium of demand and supply is altered and the tax is diffused by a process of bargaining among all those whose decisions influence prices. Some part of the tax may be shifted back to the producers, some of it may stick with the traders, while much of it is transferred forward to the consumers. In the process of diffusion, all producers, traders and consumers, not only of the product in question, but also of related and competing products, will be affected. The ultimate effects of a new duty are clearly in the direction of raising import prices and reducing import quantities, but the actual degree to which those prices will be raised and quantities reduced, as well as the extent of the divergence created between prices in the exporting and importing markets, varies considerably with the particular circumstances of the commodity taxed, and the general circumstances of the time. But the compensatory adjustments that are always at work in the price

¹ Cf. the discussion of the effects of quotas in France by M. Adéodat Boissard, Inspector of Finance, in *Journal Officiel de la République française*, Annex 24, December 1932, pages 1476 and 1477.

system spread these effects over producers and consumers of a large variety of commodities and over the trade passing with more than one country. A tariff therefore has to be very high before it opens an unbridgeable gap between the prices of the same commodity in different markets, and affects a violent reduction in the quantity of commodities traded. Its effects in these directions are smoothed over by price adjustments that tend to create a new equilibrium.

The new quantitative restrictions, such as quota systems, on the other hand directly limit the imports of particular commodities. From that limitation there is no escape by way of price adjustment—the trade is simply stopped. When such restrictions are as drastic and widespread as they have recently become, the inevitable result is an unprecedented reduction in the quantum of trade. The converse of this reduction is a piling up of commodity stocks despite the extremely adverse price relationships upon which the raw material exporting countries are forced to trade.

At the same time, the various domestic markets are cut off from one another and prices vary between them to an extent that has not been experienced since the development of modern methods of transport and communication. Attention has already been drawn to these price disparities.¹ How far they are caused by the raising of tariffs or by the new quantitative restrictions it is impossible to say; but, obviously, in default of the existing quotas and similar restrictions, tariffs, to achieve the same effect, would have to be raised very considerably even from their present levels.

Moreover, the effects of such price disparities and quantitative reductions upon the production of a great number of commodities are such as to create an extremely difficult international problem. The pattern of world specialisation has been re-arranged. Industrial countries have fostered their agriculture, in many cases almost to the point of self-sufficiency, while at the same time maintaining and even extending their industrial equipment. Agricultural production in the surplus-exporting countries, on the other hand, has not, in general, decreased but increased, while there is evidence that, in many of these countries, a strong trend to local industrial development has set in. Statistical evidence of these facts has been given in a preceding chapter.² In so far as trade restrictions have contributed to this disorganisation of production, they have prolonged the emergency which they were intended to combat.

¹ Chapter II.
² Chapter III.

THE DEVELOPMENT OF COMMERCIAL POLICY.

During 1932 and the early months of 1933, trade negotiations, almost wholly bilateral in character, occupied an increasing share of the activities of Governments in international affairs. The number of bilateral treaties negotiated has been so great that any short summary of them is impossible in the space available here. Treaties, trade agreements and exchanges of notes, generally of a limited character covering the trade in certain specific commodities for a brief period of time, have followed each other in rapid succession. Not a month passes without the announcement of several new treaties or provisional agreements, most of which refer to specific and often temporary arrangements, generally terminable at short notice, regarding a comparatively few commodities. Such arrangements defy any attempt at brief summary ; but certain tendencies common to most of them may usefully be stated here.

The first fact to be noticed is the absence of multilateral negotiations, except in the cases noted below of regional agreements between countries that are closely connected either by neighbourhood or by economic relations. The circumstances of recent months have been unfavourable to the conclusion of general accords based upon broad principles of international agreement. The Convention negotiated in 1928 for the abolition of prohibitions and restrictions on imports and exports, which had been signed by twenty-nine countries, did not come into effective operation, since nine countries failed to ratify it and twelve of the remaining twenty made their ratifications conditional upon others which were not, in fact, received. Unilateral action continued, but was increasingly followed by bilateral agreements. Treaties or accords were denounced, or tariffs raised ; but in the great majority of cases such unilateral action was followed quickly by negotiations, which resulted in at least provisional agreements with the other countries concerned. More and more the regulation of trade took of the form of specific agreements between particular countries, generally after consultation with, and often after direct negotiation between, the industrial and trading interests in both countries.

The greater number of the bilateral agreements thus arrived at were frankly temporary, short-term compromises reviewable at short notice, designed to make possible the continuance of at least a minimum of foreign trade, but avoiding more permanent commitments until economic circumstances should become more favourable. There was a general disposition to maintain liberty of action for the future, and, indeed, to secure greater liberty

by the de-consolidation of tariffs that had been fixed by former agreements. There were notable exceptions, such, for example, as the treaties negotiated by the Soviet Government with Germany in May, and with France in November 1932. Against this increase of economic co-operation between the U. S. S. R. and other countries must, however, be set the denunciation by the United Kingdom in April 1933 of the British-Soviet agreement of 1930, and the imposition of embargoes both by the United Kingdom and by the U. S. S. R.

New forms of trade bargaining have entered into many of the provisional bilateral agreements. Not only tariff provisions, but quotas and similar arrangements for quantitative trade regulation, purchasing agreements, understandings between organised industrial interests in the respective countries, and financial considerations, such as debt settlements and loan provisions, have been incorporated into the new treaties. While such arrangements were not unknown before the depression, they were the exception rather than the rule. The extent to which they have become the subject of official negotiations is so great as to constitute a development of commercial policy which is likely to exert a profound influence in the future.

Trade negotiations in the past have generally followed the comparatively simple method of bargaining upon tariff schedules, any reductions of duties being extended in most cases to other countries than those immediately concerned by the operation of most-favoured-nation clauses. Industrial organisation, as well as trading and financial arrangements, were affected by such negotiations only indirectly, competitive enterprise being left free to adjust itself to the altered tariff conditions. This freedom of competition, aided by the generalised effect of most-favoured-nation treatment, in practice meant that a country's commercial policy was affected by its whole external trade rather than its exchanges with another country. Little if any consideration was given, before the depression, to the balance of trade between particular countries, and domestic industries were protected against imports in general rather than imports from a particular source.

In recent years, however, the structure of industry and the nature of world trade have been changing considerably. Manufacturing industries are no longer confined to a comparatively few countries. The development of modern industrial organisation and the growth of an international financial system have rendered possible the development of a wide range of manufactures in an increasing number of countries. International trade before the depression had included more interchanges of manufactured goods and depended less upon the exchange of

manufactures for raw materials. To an increasing extent, also, the organisation of production, and particularly of manufacturing production, began to transcend national boundaries. International combines and international firms, facilitated by the increasing ease with which credit could be transferred from one country to another, greatly complicated the working of protective tariffs. The extent to which the export of goods was being replaced by the export of industries is difficult to estimate ; but sufficient information exists to show that it is becoming an important factor in altering the character of international trade.¹

It is possible that such changes in industrial structure and trading organisation might not have brought any sudden alteration in commercial policy if the depression had not produced such minute and detailed regulation of trade. Since, however, the temporary trading agreements of the last two years have, in fact, attempted to regulate, not only tariffs, but also the partition of markets and therefore the localisation of production as well as the financing of industry and trade, it seems likely that commercial policy in the future will be directed more definitely along such lines than along the older lines of general tariff agreements. Already important new treaties are taking this form.

Two characteristics of these new treaties, exemplified both in the Ottawa agreements and in those recently negotiated by the Government of the United Kingdom with Denmark, Sweden, Norway, Iceland and the Argentine, deserve special mention. There is, in the first place, a clear tendency towards the formation of regional groupings. The extension of the methods followed at Ottawa to negotiations with other countries which have close trade relations with the United Kingdom is characteristic of the process. The French Government is also proceeding actively to plan closer trade relations with its colonies.² The Canadian and United States Governments are negotiating a trade treaty upon lines similar to those worked out at Ottawa. In Europe, there are preferential agreements negotiated by Estonia with Finland, Latvia and Lithuania ; the various forms of preferential treatment, first by export premiums and later by quota arrangements, between Austria and Hungary (July 1932) ; the arrangements for mutual export credits and reduced railway tariffs negotiated by Italy with Austria and Hungary ; a preferential agreement between France and Yugoslavia

¹ Cf., e.g., Frank A. Southard, Jr. : " American Industry in Europe ", Houghton Mifflin Company, Boston, 1931 ; a study of almost 800 subsidiaries in Europe of 220 American corporations.

² Cf. *Journal Officiel de la République française*. Annex 24, December 1932, pages 1474 and 1475.

(November 1931) and the Oslo agreement between the Scandinavian countries, the Netherlands and Belgium. More ambitious schemes for regional Customs agreements in Central and South-eastern Europe, such as those outlined at the Stresa Conference, while not yet translated into agreements, indicate the same tendency to regional grouping.

The second characteristic, particularly of the Ottawa treaties, is the tendency to seek agreements for the fostering of "complementary production". The older free trade initiative took the form of agreement, generally among low-tariff countries, for further reductions of duties the benefits of which accrued to the whole trading world by reason of most-favoured-nation treatment. The new development of commercial policy is based, theoretically, upon a rough planning of industrial development with the intention of discouraging the less and encouraging the more efficient forms of production in each country.

The working out of such principles by a series of bargains between each pair of countries is obviously a laborious and difficult process, especially when it is complicated by financial as well as industrial and trading considerations. The slowness and incompleteness with which bargains are worked out may involve a maintenance of a large part of the existing trade barriers for a considerable time. Moreover, the effort to balance a country's trade as far as possible with every other country renders exceptionally difficult the position of those countries which are most dependent upon triangular trade. It is only by accident that a particular country finds that its best export market is also the cheapest market from which it can import and the most convenient source of its capital supply. There is also, as in all schemes for Government control or regulation, the danger that planning may involve the suppression of private initiative in such a degree as to impair industrial progress. An increased tendency towards cartellisation and a greater degree of governmental control over industry and trade would also seem to be likely if commercial policy should continue to follow this line of development.

Up till the present, the great majority of the new bilateral treaties and trade agreements have continued to stipulate most-favoured-nation treatment; but, in fact, the scope of such treatment has been greatly modified. Apart from the emergency restrictions such as quotas and exchange controls, which raise new and difficult questions of interpretation, special bilateral or regional treatment has in fact been secured by such methods as the negotiation of industrial understandings which are "taken note of" in the treaties. Exceptions have always been recognised even to the unlimited and unconditional interpretation of the

The great bulk commodities which are shifted from country to country after the harvest period always bring up the percentages in the second half of the year. While the prices of these commodities have fallen very heavily, the quantum has been maintained better than the quantum of manufactured products.

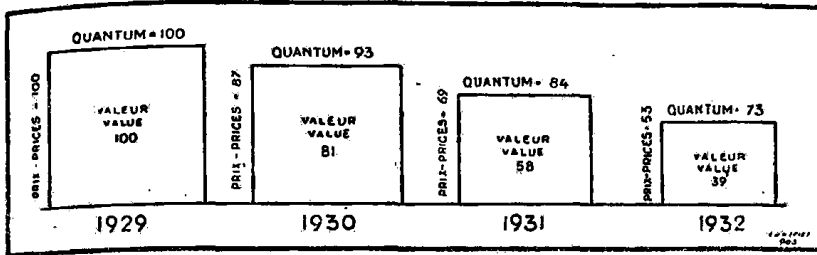
The decline in total values is compounded of these two elements — a sharp fall in prices and a substantial decline also in the actual quantum of goods traded. Both have been continuously accelerating, except for the partial and temporary recovery of prices of certain commodities in the autumn of 1932. Correction of total values for price changes in order to arrive at estimates of the quantum of trade are subject to certain statistical limitations which lessen their accuracy as the base year recedes.¹ The calculations made by the Economic Intelligence Service of the League of Nations indicate that, in 1930, the quantum was about 7 per cent less than in 1929, and that it fell again in 1931 by 9 to 10 per cent and, in 1932, by 14 per cent, the total decline in the quantum for 1932 therefore being 26 to 27 per cent from the levels of 1929. Since, however, the quantities of those goods — agricultural products in particular — which have fallen most in price have not diminished as much as the quantities of other goods, it is probable that the estimates given above understate the fall in the total quantum and overstate the average fall in prices. The true position may perhaps be summarised roughly by the statement that seven-tenths of the goods traded in 1929, changing hands at rather more than half the prices current in 1929, gave a total value of world trade in 1932 less than 40 per cent of the value in 1929.

Such a statement, approximate as it must remain, emphasises the unprecedented shrinkage in the actual quantities of trade passing, a shrinkage primarily caused by the accumulated trade restrictions described in the preceding pages. The combined effects of the fall in prices and in quantum may be illustrated graphically by the following diagram in which prices are measured vertically and quanta horizontally.

It has already been indicated that the greater part of the quantitative decline has taken place in manufactured goods rather than in agricultural foodstuffs and raw materials. The existence of large surplus stocks of commodities, however, is sufficient evidence that the growing restrictions on trade have reduced even the basic interchange of raw materials and foodstuffs to levels that are too low to carry off the production. World agricultural production, it has been shown, has not seriously decreased, but manufacturing production has fallen away very

¹ Cf. *Review of World Trade, 1932*, pages 20-1.

The Fall in World Trade, 1929-1932.



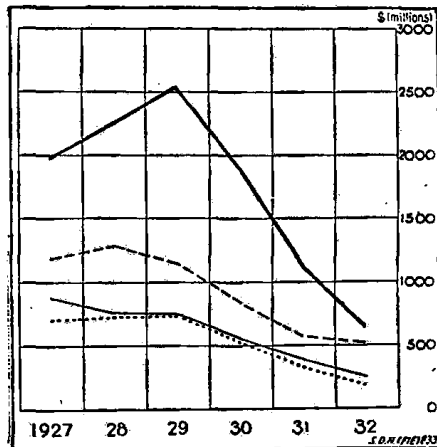
greatly, and it is clear that increased trading restrictions form one of the primary reasons for this decrease. What has been happening, therefore, is a drastic reversal of the processes described in last year's *Survey* as typical of modern economic development before the crisis. Instead of an increasing super-structure of specialised interchange of a growing variety of manufactured products, the world is being driven back to a minimum level of trade in the barest necessities.

The statistics that are available to indicate the geographical distribution of trade confirm this conclusion. It is in the United States, and particularly in the exports of manufactured articles from that country, that the export trade has declined most.

The obverse fact is clear also, that the exporting agricultural countries, while on the whole maintaining and even extending their export quantities, have received much lower prices and

*United States :
Domestic Exports by Groups
of Commodities.*

Recorded
Annual Values.



- Foodstuffs.
- - - Crude materials.
- Semi-manufactures.
- Finished manufactures.

therefore have taken less and less imports from the industrial countries. These facts become clear in the following table, which, for the years 1930-1932, shows the percentage decline of import and export values for about forty countries, representing about 90 per cent of the total value of world trade.

The Percentage Decline in Import and Export Dollar Values since 1929.

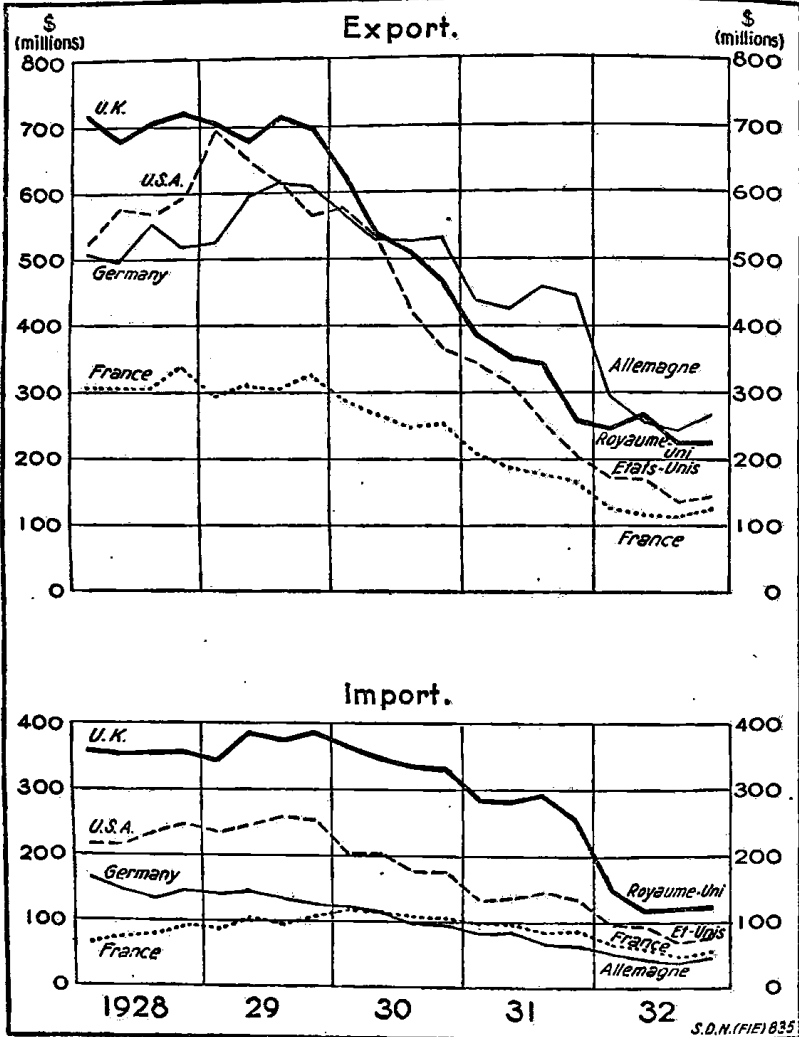
Country	Imports			Exports		
	1930	1931	1932	1930	1931	1932
	%	%	%	%	%	%
Chile	14	56	87	42	64	84
Peru	33	62	78	28	58	67
Brazil	38	65	75	31	48	61
Argentine	25	57	74	43	53	64
Australia	35	72	74	29	47	55
Uruguay	16	32	73	5	51	71
Poland	28	53	73	14	33	62
Finland	25	53	70	16	35	56
Canada	22	53	69	26	49	60
United States of America	28	52	69	27	54	69
British Malaya	20	51	69	29	59	75
Hungary	23	49	68	12	45	68
Mexico	10	50	67	24	41	65
New Zealand	12	53	66	21	46	58
Germany	23	50	65	11	29	58
Austria	17	34	65	16	41	71
Yugoslavia	9	37	65	14	40	64
Egypt	14	47	64	39	53	64
Ceylon	25	49	64	23	48	67
Spain	+11	57	64	+ 9	54.5	65
Czechoslovakia	21	41	63	15	36	64
Italy	20	46	63	20.5	34	57
Greece	21	33.5	62	17	40	61
India	25	49	61	22	53	70
South Africa	22	37	60	14	27	29
Japan	26	41	60	27	44	60
Roumania	22	47	60	2	24	43
United Kingdom	14	34	58	22	50	64
China	26	40	57	37	52	75
Norway	1	25	57	9	43	49
Sweden	7	25	56	15	42	64
Denmark	3	23	55	6	27	53
Belgium	13	33	54	18	27	53
Netherlands	12	31	53	14	34	57
Irish Free State	7	23	50	5	28.5	60
France	10	27	49	15	39	61
Switzerland	5.5	17	36	16	36	63
Algeria	3	17	27	+10	12.5	3
U. S. S. R.	+20	+25	21	+11	14	40

The countries are arranged in order of the magnitude of the fall in imports in 1932. If they were arranged in the order of the fall in exports, many of the industrial countries would come higher, while the agricultural countries would mostly be found towards the bottom of the list.

There is, in addition to this structural difference in economic organisation, a distinction to be drawn between debtor and creditor countries. For the most part, the agricultural exporting countries are also the greatest debtors ; but there are exceptional cases, such as that of Germany, which is primarily an industrial country but is heavily indebted on international account, and that of the United States, which is a great creditor country but maintains also an active export balance with both industrial and agricultural commodities entering into it. Industrial exports have fallen off heavily, while agricultural exports have suffered severe price declines but have been fairly well maintained in quantity. The oft-quoted inconsistency of the various factors in the American trading position has therefore not been removed by the crisis. The balance of commodity trade is still active, and vigorous efforts have been made to promote both manufactured and agricultural exports, while imports are being checked by the high tariff and investment and debt claims maintained without renewing capital exports.

Exports and Imports of Manufactured Articles.

Recorded Trade Values (by Quarters) for the United Kingdom, the United States of America, Germany and France.¹



¹ It should be observed that the comparison is based on available information concerning the value of manufactured goods according to the main groups of national classifications (in the case of Germany the international (Brussels) classification) as shown in national trade returns. Although these data are not strictly comparable, owing largely to a different classification of certain semi-manufactured products, the diagram claims to show adequately the trend of the countries concerned.

Apart from such exceptions, however, it may be stated generally that the terms of trade have continued to run unfavourably to the agricultural exporting debtor countries.¹ Any recovery of world prices which is to remedy this disequilibrium must begin with increased demand and higher prices for raw materials and foodstuffs in the industrial countries. Only in this way can the agricultural debtor countries improve their balances of payments, while extending their imports.

In the meantime, there is evidence that the trade war which has been raging, particularly among the industrial countries, is having somewhat similar effects to those which followed the war of 1914-1918. Trade is decreasing almost universally; but its geographical distribution is shifting considerably as the next table shows.

The Percentage Distribution of World Trade by Continental Groups.
(Basis: Recorded values, reduced to dollars; special trade, merchandise only.)

Continental Group	Imports				Exports				Total			
	1929	1930	1931	1932	1929	1930	1931	1932	1929	1930	1931	1932
Europe, excl. U.S.S.R.	54.2	56.4	58.4	58.1	47.2	50.2	51.2	48.8	50.8	53.5	55.0	53.7
Europe, incl. U. S. S. R.	55.4	58.3	61.1	60.7	48.6	52.2	53.4	51.1	52.1	55.4	57.5	56.1
North America . .	16.0	14.3	13.1	12.6	19.5	17.9	16.1	16.5	17.6	16.0	14.5	14.5
Latin America . .	7.6	7.2	5.8	5.5	9.6	8.5	9.0	9.2	8.6	7.8	7.4	7.3
Africa . . .	4.8	5.1	5.4	5.7	4.5	4.6	5.0	6.4	4.7	4.9	5.2	6.0
Asia, not including Asiatic Russia . .	13.5	12.7	13.0	13.5	15.1	14.3	13.9	13.7	14.3	13.5	13.4	13.6
Oceania . . .	2.7	2.4	1.6	2.0	2.7	2.5	2.6	3.1	2.7	2.4	2.0	2.5
Total . . .	100	100	100	100	100	100	100	100	100	100	100	100

While the lack of homogeneity among the countries in some of these continental groups renders the interpretation of the

¹ Cf. Chapter II.

figures difficult, the more detailed information available for individual countries leaves little room for doubt that very considerable shifts in the distribution of world trade are under way.

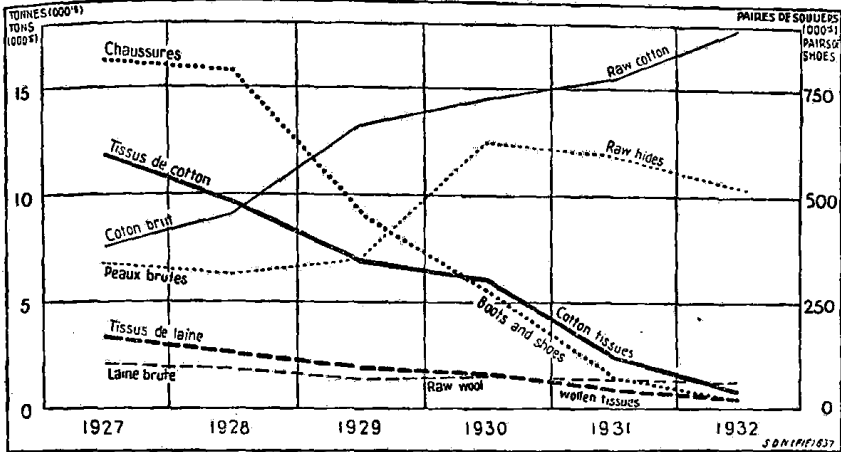
Percentage Share of Certain Countries in World Trade.

Country	1929		1932	
	Imports	Exports	Imports	Exports
United Kingdom	15.19	10.74	16.43	10.06
United States	12.19	15.61	9.58	12.39
Germany	9.00	9.72	7.98	10.70
France	6.41	5.95	8.44	6.08
Canada	3.65	3.71	2.87	3.83
Netherlands	3.11	2.43	3.77	2.68
Belgium	2.77	2.68	3.26	3.23
Japan	2.81	2.93	2.84	3.05
Italy	3.20	2.42	3.05	2.73
India	2.54	3.54	2.53	2.79
U. S. S. R.	1.27	1.46	2.59	2.28
Argentina	2.30	2.74	1.55	2.59
China	2.27	1.97	2.48	1.26
South Africa	1.19	1.37	1.21	2.53
Switzerland	1.45	1.21	2.39	1.17
Australia	1.98	1.79	1.35	2.10
Czechoslovakia	1.66	1.83	1.59	1.70
Dutch East Indies	1.25	1.76	1.15	1.82
Sweden	1.34	1.47	1.53	1.37
Spain	1.48	1.23	1.35	1.11
Algeria	0.65	0.46	0.20	1.16
Brazil	1.19	1.39	0.76	1.41
British Malaya	1.40	1.58	1.11	1.03

It is evident that, with certain exceptions, the share of the reduced world trade claimed by industrial countries was greater in 1932 than in 1929. This, however, was because of an increase in their imports. Thus, British imports rose from 15.19 to 16.43 per cent, French from 6.41 to 8.44 per cent, Dutch from 3.11 to 3.77 per cent, Belgian from 2.77 to 3.26 per cent, Swiss from 1.45 to 2.39 per cent. The exceptions are numerous — in the United States, Germany and Canada, for example, imports declined heavily. On the other hand, the decline of imports in the agricultural countries is very widespread. The strong tendency towards increased industrial equipment in countries hitherto dependent upon imported manufactures which has been mentioned in an earlier chapter, is the counterpart of these trade movements. The reversal of capital flow, adverse terms of trade, and growing trade restrictions have tended to promote autarchic developments

in the agricultural as well as the industrial countries. The natural corollary to agricultural protection in industrial countries is industrial development among the agricultural peoples who have been their customers. The *Review of World Trade, 1932*, gives some clear illustrations of such developments.

Hungary : Imports of Certain Raw Materials and Manufactured Articles.



The currency instability which has been a marked feature of the last year is a further factor of great and disturbing importance in world trade. Competitive currency depreciation, even when it is reluctantly entered upon, is a most formidable weapon of economic warfare ; but, unfortunately, it tends to have a boomerang effect, returning to strike dangerously at the spot from which it started. The beautiful simplicity of a policy which aims at lowering export costs by allowing a managed currency to depreciate externally, while at the same time endeavouring to maintain internal price stability, becomes obvious to exporters in more than one country. As one example of the way in which such a policy spreads there may be cited the chain of events which followed the depreciation of the New Zealand pound in January 1933. Despite its heavy external commitments, the Government brought pressure on the banks to raise their buying rate for sterling to the same level as that which had been in force in Australia since the beginning of 1931 — viz., 25 per cent premium. This measure was prompted by local considerations and was part of a considered plan to relieve the agricultural exporters. But the international repercussions

were immediate. Within a few days, Denmark, the chief rival of New Zealand in the English butter market, allowed the krone to drop to approximately the same level. Shortly afterwards, the Canadian Government initiated friendly conversations with New Zealand in order to avoid the necessity of imposing exchange dumping duties upon butter, which had only a short time before been the *casus belli* in a trade war between the two dominions. Almost at the same time it so happened that the British Government, as part of its plans for agricultural reorganisation, consulted the dominion and foreign producers concerning the possibility of imposing a butter quota. All of these actions were taken purely for reasons of domestic policy, without any intention of instituting reprisals. However, the price of butter in London went down substantially and the advantage accruing to the New Zealand exporter was minimised, with a more permanent possibility of his markets being restricted.

This instance is cited merely by way of example. Similar developments of the immediate reactions to currency depreciation might be cited from the experience of sterling, the depreciation of the yen, or the abandonment of the gold standard by the United States of America. The disturbance of international prices which results as one currency after another leaves gold sets up a scramble for trade advantages in which the chief weapons are higher import tariffs and quotas on the one hand, deflation in gold countries and further currency depreciation in paper countries on the other hand.

Chapter VIII.

MONETARY AND CREDIT POLICIES.

THE INSTABILITY OF THE EXCHANGES.

It was stated in the first chapter of this *Survey* that exchange instability resulting from the breakdown of the international gold standard was one of the principal causes of further economic deterioration in 1932 and figured prominently among the factors which limited and checked the revival of prices and productive activity in the third quarter of that year. In the previous *Survey*, attention was paid to the more fundamental economic forces which threw the principal national price systems out of equilibrium and rendered the task of keeping the exchange rates stable so difficult as to drive one country after another off the gold standard.¹ The earlier stages of this abandonment of the international standard were also described, and note was taken of the fact that, in the middle of 1932, there were some indications that the financial panic which began a year earlier was easing off, but had left economic activity at a low ebb.² At that time, however, the secondary consequences of exchange instability were not fully apparent, and it is necessary therefore to record the events since June 1932.

The extent to which the international gold standard had broken down by the middle of 1933 is summarised in the following tabular statement showing the important dates in the development of monetary policies since the depression.

It should be noted that, in many of the countries which retain the nominal gold parity for their currencies, the measures adopted for dealing with the blocked accounts that are accumulated as the result of exchange controls and transfer moratoria create in effect subsidiary exchange rates for special purposes.

¹ *World Economic Survey, 1931-32, Chapters I and II.*

² *Ibid.*, Chapter XI.

THE DEVELOPMENT OF MONETARY POLICIES SINCE THE
DEPRESSION. ¹

The Abandonment of the Gold Standard.

Date of depreciation in relation to gold		Country	Official suspension of gold standard ¹	Official imposition of exchange control ²
Year	Month			
(Countries whose Currencies have depreciated in relation to Gold.)				
1915 . . .	—	Turkey	5	26. II. 30
1920 . . .	—	Spain	5	18. V. 31
1929 . . .	IV	Uruguay	XII. 29 ⁵	7. IX. 31
	XI	Argentina	16. XII. 29	10. X. 31
	XI	Paraguay	9	VIII. 32
1930 . . .	XII	Brazil	—	18. V. 31
	III	Australia	17. XII. 29	—
	IV	New Zealand	1. I. 32 ⁵	—
	IX	Venezuela	—	—
	X	Bolivia	25. IX. 31	3. X. 31
1931 . . .	VIII	Mexico	25. VII. 31	—
	IX	United Kingdom	21. IX. 31	—
	IX	Denmark	29. IX. 31	18. XI. 31
	IX	Canada	19. X. 31	—
	IX	Egypt	23. IX. 31	—
	IX	India	21. IX. 31	—
	IX	Ireland	26. IX. 31	—
	IX	British Malaya	21. IX. 31	—
	IX	Norway	29. IX. 31	—
	IX	Palestine	21. IX. 31	—
	IX	Sweden	29. IX. 31	—
	X	Austria	(5. IV. 33) ³	9. X. 31
	X	Finland	12. X. 31	—
	X	Portugal	31. XII. 31	21. X. 22
1932 . . .	X	Salvador	8. X. 31	—
	XII	Japan	13. XII. 31	1. VII. 32
	I	Colombia	21. IX. 31	21. IX. 31
	I	Costa Rica	5	16. I. 32
	I	Nicaragua	—	13. XI. 31
	III	Persia	10	—
	IV	Chile	20. IV. 32	30. VII. 31
	IV	Greece	26. IV. 32	28. IX. 31
	V	Peru	18. V. 32	—
	VI	Ecuador	9. II. 32	30. IV. 32
1933 . . .	VI	Siam	11. V. 32	—
	VII	Yugoslavia	12	7. X. 31
	I	South Africa	28. XII. 32	—
	IV	United States of America	6. III. 33	6. III. 33
	IV	Guatemala	—	—
	IV	Honduras	7	7
	IV	Panama	6	6
VI	Philippines	7	7	
	VI	Estonia	28. VI. 33	18. XI. 31.

¹ League of Nations, *Monthly Bulletin of Statistics*, July 1933.

Country	Official suspension of gold standard ¹	Official imposition of exchange control ²
(Countries whose Currency remained at Gold Parity at End of July 1933.)		
Albania	—	—
Belgium	—	—
Bulgaria	—	—
Czechoslovakia	—	15. X. 31
Danzig	—	26. IX. 31
Dutch East Indies	—	—
France	—	—
Germany ¹³	—	13. VII. 31
Hungary ⁸	—	17. VII. 31
Italy	—	—
Latvia	—	8. X. 31
Lithuania	—	—
Netherlands	—	—
Poland	—	—
Roumania ⁴	—	17. V. 32
Switzerland	—	—
U. S. S. R.	—	11

For example, in Germany, the following classes of blocked accounts are recognised: foreign mark claims accumulated before July 16th, 1931, but not subject to the standstill agreements (Altguthaben), foreign property claims acquired after August 3rd, 1931 (Kreditspermark), bank-notes brought into Germany after February 19th, 1933 (Notenspermark), claims

¹ Or embargo on gold export.
² Unofficial restrictions are disregarded.
³ Since April 6th, 1933, all exchange transactions have been carried out at free market rate.
⁴ Gold exports prohibited July 28th, 1933.
⁵ Costa Rica, Spain, Turkey, New Zealand, Uruguay: the gold standard has not been legally established since the war; the latter two, however, reverted *de facto* to the gold parity.
⁶ The United States dollar in use also in Cuba, the Dominican Republic, Haiti and Panama, which have no comprehensive currency system of their own.
⁷ Honduras, Philippines: dollar exchange standard.
⁸ Since December 1932, the exporters of certain agricultural articles obtain a premium ranging from 3 to 20 per cent in addition to the pengö parity equivalent of foreign exchange surrendered to the National Bank, and importers have to pay a surcharge ranging from 13.5 to 17 per cent over and above the parity of exchange.
⁹ Paraguay: Argentine peso exchange standard.
¹⁰ Persia: silver standard until March 1932, when a gold parity was legally adopted. The exchange rate, however, approximately followed the £ sterling.
¹¹ U. S. S. R.: State monopoly for foreign exchange transactions.
¹² Official domestic quotations maintained in the neighbourhood of gold parity. Since October 17th, 1932, however, a premium of 20 per cent has been fixed by the National Bank for all transactions with countries with which no clearing agreement exists. In the clearing agreements, the premium has been fixed as from January 2nd, 1933, at 28½ per cent.
¹³ For recent developments in connection with blocked mark accounts in Germany, see pp. 223-4.

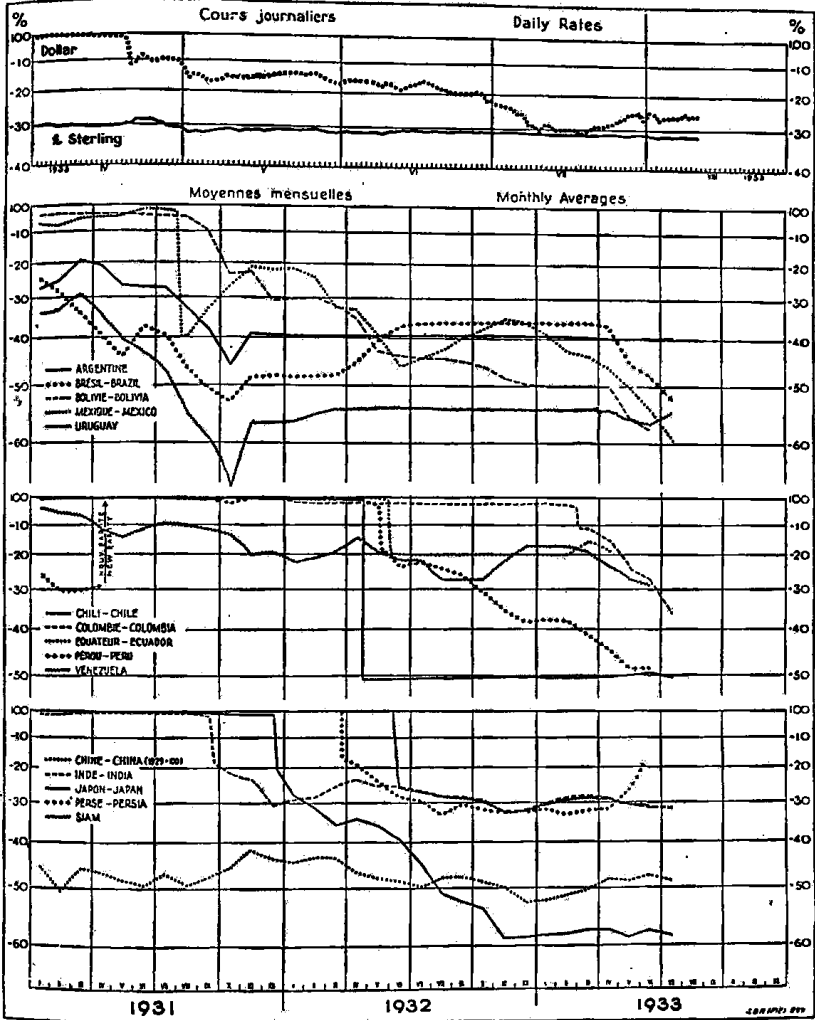
created by the sale or redemption of stocks and bonds (Effectenspermark). Scrip issued in even amounts, with a minimum of RM. 40, may be issued to the owners of Konversionsspermark and marketed on German and foreign stock exchanges. All of these blocked marks can be used, with the consent of the Exchange Control Office (Devisenbewirtschaftungsstelle), to buy mortgages or fixed property, or to give credit to Germans in Germany, or to share in a German enterprise, provided always that the investment is for five years at least. Under certain conditions, also, they may (except in the case of Effectenspermark) be used to pay for purchases of German commodities destined for "supplementary exports". The price paid for such blocked marks varies with the uses for which permission is given. At the end of July the current values ranged from about 28 per cent to 37 per cent (Effectenspermark) below the gold parity. In the same way, tourists may buy blocked marks below the official rate. The credits subject to the standstill agreement of February 1933 (Registermark) may also be used extensively for certain purposes within Germany at about the same parity. Finally, the blocked marks now being accumulated as the result of the transfer moratorium on interest and amortisation payments on long-term loans which began on July 1st, 1933 (Konversionsspermark), will provide another large amount of currency valued below gold parity. On the other hand, German exporters who have acquired the right to make "supplementary exports" may use part of the proceeds to buy German bonds abroad and re-sell them in Germany. This right is marketable and its value depends mainly upon the relative prices of German bonds at home and abroad. In July 1933, the value was about 20 per cent of the foreign price of such bonds.¹

In order to illustrate the confusion of the exchanges during the greater part of 1932, the following diagrams are presented. They give a graphic picture of the way in which one currency after another fell from its gold parity. It is very clear, however, that, in the second quarter of 1933, rates were relatively stable, sterling keeping a constant relationship to the gold currencies, and other paper currencies remaining fairly stable in relation to sterling and to gold. There was evidently a strong tendency until the depreciation of the dollar began late in April towards settlement at a new exchange equilibrium. Whether the measure of equilibrium that had been reached can be maintained is a question that must be left for the next few months to answer.

¹ Cf. "Die Sperrmarksorten" in *Frankfurter Zeitung*, July 23rd, 1933.

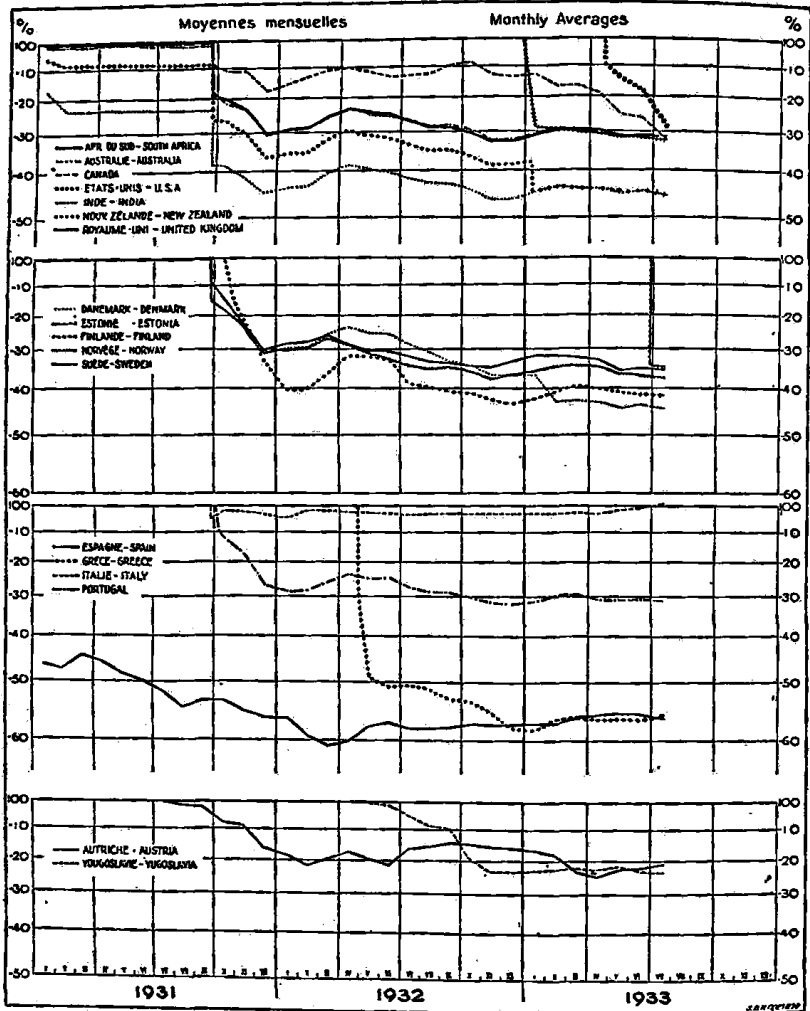
Exchange Rates.

PERCENTAGE DISCOUNT OF CERTAIN CURRENCIES IN RELATION TO THEIR GOLD PARITY.



Exchange Rates.

PERCENTAGE DISCOUNT OF CERTAIN CURRENCIES IN RELATION TO THEIR GOLD PARITY.



The grouping of the countries in the table on pages 222-3 emphasises the obvious importance, first, of the sterling depreciation in September 1931 and, later, of the dollar depreciation in April 1933. There were, in fact, three main currency groups in the world at the middle of 1933 — the gold bloc, the sterling bloc, and the dollar with its dependent currencies. This grouping became very clear during the course of the Monetary and Economic Conference. When it became apparent that, because of the developments of domestic policy in certain countries, immediate currency stabilisation was unlikely, there was a strong tendency for the countries remaining on gold, together with many other European countries which supported their policies, to seek closer means of monetary co-operation. In the only vote actually recorded on the financial side of the Conference, fifteen European countries supported the policy advocated on behalf of the gold bloc. Among these were to be found, not only the gold countries proper, but others which were either off the gold standard or maintained their currencies at nominal gold parities only by exchange controls.¹ In addition the gold countries, at a meeting in Paris of Central Bank representatives early in July, adopted concerted measures to sustain the gold parities of their respective currencies.

The sterling bloc also took a more definite shape when, on July 27th, the delegations of the United Kingdom, Canada, Australia, New Zealand, South Africa and India issued a joint declaration on currency policy.² This declaration re-affirmed the Ottawa policy of cheap credit aiming at a rise in prices, and re-stated the "ultimate aim of monetary policy" as "the restoration of a satisfactory international gold standard under which international co-operation would be secured and maintained with a view to avoiding, so far as may be found practicable, undue fluctuations in the purchasing power of gold". The declaration further recognised "the importance of stability of exchange rates between the countries of the Empire in the interests of trade", and opened the door for co-operation in this respect from other countries by the statement that "the adherence of other countries to a policy on similar lines would make possible the attainment and maintenance of exchange stability over a wider area".

The relationship between these two definite currency groups had for some time been maintained stable by the fact that, since February 1933, sterling had remained at a constant level in

¹ The fifteen countries were Germany, Austria, Belgium, Bulgaria, Spain, France, Italy, Lithuania, Netherlands, Poland, Roumania, Switzerland, Czechoslovakia, Turkey and Yugoslavia.

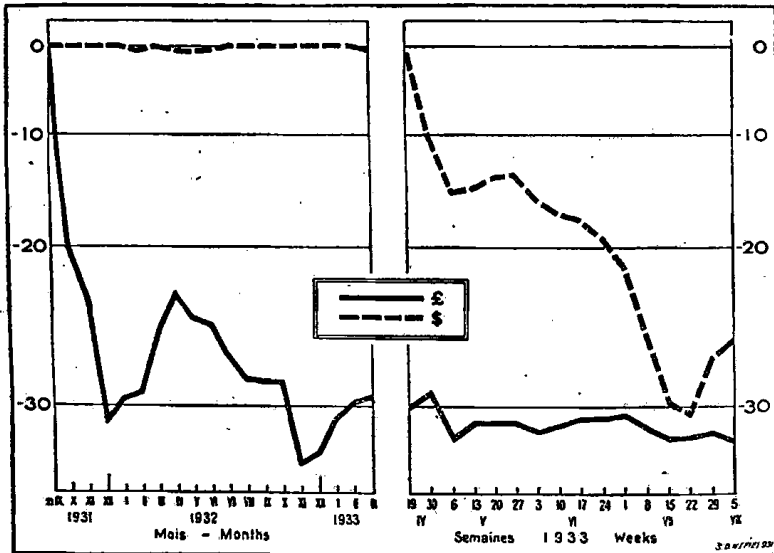
² London *Times*, July 28th, 1933.

relation to the French franc. The British Commonwealth declaration quoted above made it clear that this was not the result of any definite agreement and that "the United Kingdom Government has no commitments to other countries as regards the future management of sterling and retains complete freedom of action in this respect". The actual stability of the sterling group exchanges relatively to the gold currencies for the six months preceding the declaration is, however, a fact of considerable significance.

The remaining currency group consists of the United States dollar and its satellite and dependent currencies, mainly those of certain Central American republics and the Philippines. The Canadian dollar inevitably occupies a position midway between the sterling and the dollar groups. The fluctuations of the dollar exchange in the months following the abandonment of the gold standard on April 19th, 1933, were both violent and rapid. After touching parity with sterling (\$4.87 to the £) in mid-July, the value of the dollar appreciated again, and, by the end of July, was approximately 10 per cent above sterling once again. The

*Dollar-Franc and Sterling-Franc Exchange Rates,
September 1931 to July 1933.*

(Percentage discount in relation to gold parities.)



fact that very wide powers of an inflationary character had been vested in the Executive, and that it was not possible to foresee what, if any, use would be made of them in the effort to force through a programme of domestic recovery, made the future prospects of the dollar exchange more than usually uncertain.

The relationship that has existed since September 1931 between the major currencies representative of the three groups distinguished above is shown by the preceding diagram. Apart from the recent sudden fall of the dollar, the most significant movement disclosed is the prolonged weakness of sterling between April and November 1932.

The factors that will govern the course of these principal exchanges during the second half of 1933 are, however, unpredictable. Government policies, movements of capital, the dispositions taken in regard to the shifting of the crops in the late summer and autumn and price movements all enter into the problem. Upon the outcome of these complex forces will depend the possibility of maintaining and extending the measure of exchange stability achieved in the first half of the year and building upon it a greater measure of international co-operation in regard to commercial as well as monetary policy. The alternative appears to be a further period of exchange instability with a renewed shock to confidence and fresh confusion in commercial relationships.

COMMERCIAL BANKING IN THE DEPRESSION.

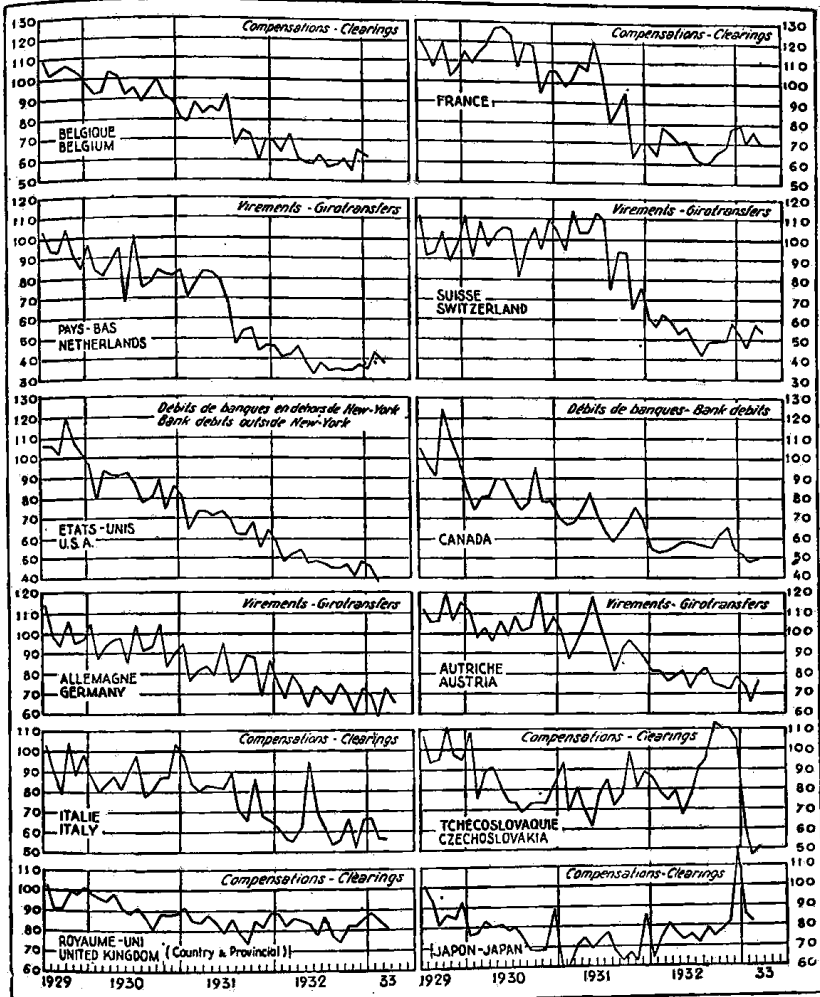
The preceding section of this chapter dealt with the extent to which national currencies and national price systems had been thrown out of equilibrium during the financial panic, and with the gradual approach to a new stability of relationships between them. The present section is concerned with certain banking problems connected with the attempt to achieve national as distinct from international equilibrium in the monetary sphere. Anything like a complete treatment of the problems involved in restoring economic equilibrium in the different countries is quite beyond the possibilities of what may be briefly attempted here; but there are certain aspects of the banking situation common to many important countries which are particularly important from this point of view. Credit is the liquid medium in which the modern industrial organisation works. The banks act as reservoirs and distributing centres for credit, and their efficiency and stability are therefore matters of the very highest importance.

The previous *Survey*, written in the second quarter of 1932, drew attention to the extreme efforts being made by the banks of most countries to preserve and improve their liquidity during the financial panic. The "liquidity crisis" was just beginning to ease off as that *Survey* was being concluded in the middle of 1932. The problems facing the commercial banks resulted primarily from the rapid expansion of credit in the years preceding 1929. In countries where the expansion, relatively to industrial activity, had been most prudent and where the traditions of banking practice had prescribed caution in lending upon any but the most readily realisable securities, the commercial banks faced the depression in a reasonably sound position. No general statement can be made as to the soundness of banking practice in one country or another. The factors to be considered are so varied and often so peculiar to the circumstances of a particular country that prolonged and detailed study is needed before any statement might be ventured in regard to individual countries. Moreover, the importance in modern economic life of international finance, and equally of international trade and price relations, is such that the financial stability of even the most prudently conducted national banking systems is likely to become involved in the difficulties created by undue credit expansion elsewhere.

As the fall of prices proceeded from 1928-29 onwards and was accelerated by the financial panic which began in the spring of 1931, and as economic activity shrank under the pressure of accumulated trade restrictions and failure of confidence, the banking systems of those countries still adhering to the gold standard necessarily sought to strengthen their liquid resources, while those which functioned in paper-standard countries were hardly less free from the need for safeguarding their liquidity. While there was, in most cases, no very great shrinkage in the nominal amounts of deposits, the velocity of circulation dropped, so that the actual usage of credit was much reduced. That this phenomenon was not confined to any particular groups of countries may be judged from the following diagram showing the shrinkage of clearings.

In view of the great shrinkage of business activity reflected by these diagrams, it is significant to find that, particularly in the countries remaining on the gold standard, the commercial banks strengthened their liquid resources, a process in which they were assisted by the lack of demand for advances. The extent to which this was achieved is shown in the table on page 232.

Monthly Clearings in Certain Countries, 1929-1933.
 (Base : Monthly Average January-June 1929 = 100.)



*Ratios of Cash Resources to Total Deposits in Certain Countries
(at End of June).¹*

Country	1929	1930	1931	1932
France	7.4	9.7	13.9	33.6
Switzerland			11.3 ^a	22.9
United Kingdom	11.3	11.5	11.7	11.5
United States	7.3	7.4	7.6	8.2
Italy	6.9	6.6	6.2	5.9
Germany	3.1	2.7	3.6	3.4
Poland	8.5	8.8	10.7	9.0
Sweden	2.1	2.3	2.1	3.8
Czechoslovakia	6.7	7.3	7.2	7.4
South Africa	10.3	10.0	9.1	10.1
Argentina	17.9	14.2	13.4	17.5
Australia	15.6	13.4	19.2	17.8
Canada	13.3	12.1	10.9	12.2
Chile	14.4	12.6	9.5	26.4
Japan	9.1	9.0	10.1	9.8
New Zealand	12.3	13.0	13.7	11.5

The movements disclosed in this table, while indicative of widely differing circumstances in the countries considered, reveal a widespread, though not universal or simultaneous, attempt on the part of banking authorities to improve their cash position. It was pointed out in the *Survey* for 1931-32 that, in the years preceding 1929, there had been, particularly in certain borrowing countries, a considerable shrinkage in the cash ratios of commercial banks as compared with pre-war practice. The margin of safety for the banks in these countries was reduced, but the recent movement has in many countries gone far towards bringing the cash ratios back to pre-war levels.

It is, unfortunately, not possible to present any measurement of the degree to which the great reductions in business profits described in Chapter V have reacted upon the liquidity of bank assets and the solvency of bank investments. It is common knowledge, however, that, during the boom period in most countries, industrial enterprises leaned heavily upon the banking systems.² Losses and frozen assets when the depression hit such industrial enterprises inevitably created a difficult series of problems for the banks.

It may be noted that the dangers arising from this situation were such that the necessity previously referred to for a strengthening of the banks' cash and liquid assets in order to safeguard depositors' interests in the event of a panic, together with the necessity for re-organising the capital structure of industry, hampered

¹ League of Nations, *Monthly Bulletin of Statistics*, No. 5, 1933.

² September 1931.

³ *World Economic Survey*, 1931-32, pages 209-211.

the first efforts by Central Banks and Governments to combat the crisis by rendering credit cheap and abundant. A clear illustration of this fact is given by the history of the United States Reconstruction Finance Corporation and of the activities of the Federal Reserve Banks briefly summarised in the next section. The mobilisation both of Central Bank and of Government credit was utilised by the commercial banks to strengthen their liquid resources in order to face the possibility of urgent demands from their depositors, and little effect was produced upon industrial activity, except that the deflationary pressure exerted by the efforts of the commercial banks to improve their liquidity by reducing their commitments was relieved.

Towards the middle of 1932, however, the efforts to mobilise credit in order to stem the deflationary pressure appeared in many countries to be on the point of achieving some measure of success. At that point in the depression it became possible to plan more fundamental measures of relief and re-organisation. That the financial situation had become easier was evident from a succession of events — the downward movement of discount rates, followed by widespread reductions of interest rates, initiated by the Bank of England in February 1932,¹ the large-scale conversions of public debt which followed, the intervention of the Federal Reserve Banks and the United States Government in the American banking situation, and not least the favourable political settlement at Lausanne.

The time was ripe to tackle the great problems involved in banking and industrial reconstruction, and particularly the liberation of the banking systems from the burden of frozen and often unrealisable assets, which was one of the main factors in preventing the abundant supply of cheap credit from penetrating to the industrial structure and stimulating a return of business enterprise.² Not only was there a widespread doubt whether the process of liquidation had been completed, but the commercial banks with large unprofitable long-term assets and much

¹ Cf. Bank for International Settlements "Third Annual Report", May 1933, page 13.

² The situation was summed up in the annual report of the Bank for International Settlements in the following passage (pages 13 and 14) :

"The reduction of money rates may, in individual countries, be attributed to a return of money from hoarding, a slight recovery in savings, a deliberate policy designed to augment bankers' balances, the acquisition of new gold by the Central Banks, or perhaps also, in some instances, to governmental action. The dominating factor of the whole movement has, however, been the lack of demand for funds due to continued stagnation in industry, commerce and the capital markets. This can also be seen from the fact that it is particularly, and often only, investments which offer the very best security on the short-term market (principally Government issues) that have primarily benefited by the interest rate reductions. It has, indeed, been singularly difficult, even when the supply of funds has been plentiful, to make the lower rates penetrate into other branches of the credit structure, and, especially, into the various categories of long-term investments."

reduced returns from short-term dealings found great difficulty in passing on to the long-term capital market the reductions in interest rates that had begun to operate in the money market. It was necessary that some steps should be taken to rid them of their frozen assets before industrial recovery could be facilitated.

The reconstruction of the German banking system, which had been especially hard hit, was begun in February when the Government, with the assistance of the Reichsbank, put into effect a plan for the thorough re-organisation of the large commercial banks, involving a considerable writing off of assets and the supply of new capital with the aid of the Treasury and, indirectly, of the Reichsbank. Towards the end of 1932, further steps were taken by the creation of two new organisations, the German Finance Institute (Das Deutsche Finanzierungsinstitut) and the Amortisation Office for Industrial Credit (Die Tilgungskasse für Gewerbliche Kredit). The former, which was created by the subscription of preference shares by a group of semi-official banks¹ and ordinary shares by the commercial banks, will take over from the latter industrial shares of solvent businesses to an amount equal to ten times the share capital subscribed by the commercial bank concerned. This bank gets rid of an illiquid asset and in return receives bills discountable, if no other market can be found, at the Reichsbank up to 75 per cent of the value of that asset. The second institution has been created in order to facilitate the writing down and re-organisation of industrial companies which cannot present a solvent balance-sheet.

The liquidation of frozen banking assets in Italy has proceeded along somewhat similar lines with less recourse to the public credit. The Italian Mobiliar Institute, created in March 1932 by the flotation of bonds on the open market, grants long-term loans to industrial companies to enable them to repay bank overdrafts. The Institute of Industrial Reconstruction, created in January 1933 by the issue of debentures carrying a State guarantee, also takes over frozen assets and so liberates the banks from pressure upon their credit resources.

The constitution of the United States Reconstruction Finance Corporation is considered in the next section. It should be noted here, however, that its work did not serve the purpose of freeing the banks from illiquid assets, but, on the contrary, tended to hypothecate their sounder assets in order to provide

¹ The Golddiskontbank, the Akzeptbank and the Bank für Deutsche Industrie Obligationen.

them with ready cash. The reconstruction of American banking activity in this respect was proceeding by individual action throughout the depression, but the panic of February-March 1933 forced both more drastic banking action and stricter Government supervision.

Action in other countries has varied. In Denmark, an institution somewhat similar to the Reconstruction Finance Corporation, the Krisefond, has been created. Austria, in March 1933, followed the German and Italian precedents by creating a separate institution, the Reconstruction Trust Company (Gesellschaft für Revision und Treuhändige Verwaltung), to take over the frozen assets from the commercial banks.

In addition to these specific cases of large-scale action to liquidate the legacies of the boom period, there have in most countries been " strenuous efforts in many branches of public and private economy to balance revenue and expenditure, to establish equilibrium between costs and prices, to render assets more liquid, to reach agreed arrangements for postponing or scaling down debt payments, to overcome the difficulties resulting from the liquidity crisis and to maintain control of the currency position ".¹ These developments, to which public authorities, central bankers, commercial bankers, and private individuals have all contributed, are at different stages in various countries ; but it is significant that the Bank for International Settlements, surveying the year 1932, should characterise it as " on the whole, a year of adaptation to changed conditions prevailing in the economic and monetary situation and one of some constructive effort ".

THE BANKING CRISIS IN THE UNITED STATES.

The general impression left by a survey of the developments analysed in the preceding section is one of gradual, if incomplete, adaptation of banking practice to the very difficult circumstances created by the financial crisis, which passed through its worst phase between May 1931 and June 1932. By the middle of 1932, though the banking systems of many countries were strained and functioning with a greatly reduced volume of business, and though there were many dangerous legacies of the crisis, such as frozen assets and heavy investment losses, most of them

¹ Bank for International Settlements " Third Annual Report ", *op. cit.*, page 6.

had come through an unprecedented period of stress, damaged, perhaps, but not destroyed. In the first quarter of 1933, however, the collapse of the United States banking system struck a fresh blow at public confidence.

The recent development, by individual enterprise, of large areas of the country, combined with a tradition of individualism and local independence, and insistence upon States rights derived from historic controversies, led naturally in the United States, as in somewhat similar periods of economic evolution in other countries, to the creation of large numbers of small, local banks, responsive to the needs of their immediate constituencies, but not fully integrated into any general financial system. The total number of banks reached its maximum in 1921, when 29,211 banks were operating; but has steadily fallen since, to 23,972 at the end of June 1929, and less than 17,000 at the end of June 1932. At the middle of 1929, 22 per cent of all the banks had a capital stock of less than \$25,000, and 84 per cent had less than \$100,000; but these 84 per cent accounted for less than 40 per cent of the total banking resources, the 250 largest banks, about 1 per cent of the total number, controlling more than half the resources. Over 80 per cent of all banks at June 1929 were situated in towns of ten thousand inhabitants or less.

The period of consolidation and co-ordination of banking enterprises had, therefore, begun long before the depression, but had not reached the point where a fully developed central banking institution was in a position to support, and in some degree control, the numerous scattered commercial banks, or where the stronger commercial banks had developed the tendency, so pronounced in other countries, to incorporate the smaller banks as branch units of the larger organisation. Branch banking had not greatly developed, and definite legal difficulties, as well as the diversity of regulation under forty-nine separate legislative bodies, presented obstacles to its extension. There was a competitive element, both in the legislation, and still more in the administrative controls, under which State and National Banks worked, and the possibility of developing an integrated financial system was greatly weakened by the advantages offered by incorporation under State laws. The Federal Reserve system, created only in 1913, discharged many of the functions of a Central Bank, but itself was on a federal basis, and did not comprehend all of the commercial banks in its activities. It did, however, bring some measure of co-ordination into the system, and the development of correspondent relationships between commercial banks went some distance also towards

linking the smaller with the larger banks, and therefore towards introducing greater elasticity of resources into the system.¹

Quite clearly, however, the banking organisation as a whole was in the early stages of transition from decentralised and unco-ordinated but vigorous local initiative to a more unified and centralised co-ordination and control. As in any financial crisis, the weaker independent units sustained the first shocks of the depression, and it was among them, particularly among the banks working under State as distinct from national regulation, and outside the Federal Reserve system, that failures were most frequent.

The difficulties which led to the financial collapse of early 1933 were, however, more fundamental than a mere structural weakness in the banking organisation. After the immediate post-war crisis, from 1922 to 1929, there had been a considerable credit expansion, in the course of which important changes in practice had the effect of impairing both the liquidity and the solvency of many institutions when the fall of security prices took place in October 1929. The credit expansion was built primarily upon the great influx of gold into the banking reserves during most of the years 1922-1929. The gold influx was supplemented by increased currency issues (for example, silver certificates) and by the liberal re-discount policies which were pursued by the Federal Reserve Banks. The impetus to business activity imparted by this increase of reserves and the cheaper credit to which it gave rise, more especially in the short-term financial markets, was greatly reinforced by the banking methods adopted to maximise both the expansion of advances and deposits based upon the newly acquired reserves and the velocity with which the credit thus created changed hands.

Without entering into the technical details of these methods, they may be rather summarily described as devices to finance the expansion of foreign business, municipal lending, and the security and real-estate speculation that developed rapidly in this period. The practice of building up time rather than demand deposits in order to take advantage of the lower reserve requirements exacted in respect of the former, the creation of security affiliates to promote the flotation and marketing of new stock issues, the practice of granting liberal advances upon industrial securities and real-estate collateral, thus facilitating the financing and re-financing of industry by direct

¹ For statistical details concerning the organisation of the banking system in the United States, see League of Nations *Commercial Banks, 1913-1929*, Geneva, 1930, and the forthcoming volume entitled *Commercial Banks, 1929-1932*, to be published at the end of 1933.

issues of new shares on the market instead of by overdrafts or commercial bills, and the provision of large loans to security brokers were some of the ways in which banking practice facilitated the security and real-estate boom. The following table, which compares the main classes of loans and investments of all commercial banks in the United States in 1922 and 1929, shows clearly the change in banking practice. It is of some interest to note in passing that the expansion of credit, and also the subsequent deflation, were greater in the "country" banks than in the great financial centres. The speculative fever was nation-wide, and pressure upon the isolated, independent country banks to facilitate expansion was very great.

Loans and Investments of Commercial Banks in the United States, 1922 and 1929.

\$(000,000's).

Class of credit	June 30th, 1922	June 30th, 1929	Increase	
			Amount	Per cent
Security loans	6,521	11,518	4,997	77
Real-estate loans	1,989	4,540	2,551	128
All other loans	15,194	18,567	3,373	22
Investments	9,215	13,191	3,976	43

The obvious corollary to such freedom of lending upon securities and real estate was an increased dependence of the banks upon the stability of the security and real-estate markets. The liquidity of the banking system as a whole, and still more of particular banks, was impaired by the decreased relative importance in their assets of self-liquidating commercial bills and Government securities and the greater importance of municipal advances and loans upon industrial securities and real estate which could not be quickly realised without undue loss in a period of difficulty. Moreover, the reduced proportion of commercial bills and Government securities in their portfolios limited the extent to which the banks could increase their liquid assets by re-discounting eligible paper at the Federal Reserve Banks. The increased proportion of their assets which took the form of direct investments was another source of illiquidity.¹ In simple language, the banks had advanced loans too freely against securities that could not be readily turned into cash

¹ Full statistical details concerning these developments will be published in *Commercial Banks, 1925-1933*.

assets without undue loss when the boom ended in October 1929. In so doing, they impaired their capacity to meet the demands of their depositors freely and adequately in the event, which actually occurred, of a financial panic.

The drastic fall of security prices and real-estate values which was precipitated by the Stock Exchange crisis of October 1929 inevitably ushered in, therefore, a period of intense difficulty for the commercial banks. It became necessary for them immediately to overhaul their portfolios, restrict their advances, call for additional collateral, and, if that was not forthcoming, realise upon the collateral already in their possession. Thus began a long period of liquidation during which the banks endeavoured to regain their lost liquidity by drastic curtailment of credit and tightening up of advances — deflationary processes that led naturally to restricted business and reduced purchasing power, necessitating further liquidation. It was this long deflationary pressure which lay behind the banking crisis of early 1933.

The phases through which the liquidation passed may be roughly divided into four periods. In the first, from the Stock Exchange break in October 1929 to the onset of the financial panic in May-June 1931, the liquidation was moderate and slow. The total decline in loans and investments of all banks between October 1929 and June 1931 was less than 7 per cent. During the early part of 1930, indeed, there was very little liquidation. Discount rates were lowered and the Federal Reserve Banks also enlarged the credit basis for commercial banks by large open-market purchases of Government securities. The indebtedness of member banks to the Federal Reserve Banks, which had been over \$1,000 million in August 1929, was, in June 1930, reduced to \$250 millions, as the commercial banks were able to sell their securities and pay off their indebtedness. These are the measures of relief ordinarily offered by a Central Bank in a crisis — free lending at cheap rates, supplemented, if necessary, by open-market purchases designed to relieve the commercial banks — but they were inadequate to correct the situation.

The crisis entered a new phase after the banking difficulties of the Austrian Credit-Anstalt in May 1931 precipitated an international financial crisis. Deflation took a sharper turn downwards in the United States and, when the United Kingdom and a number of other countries were forced off the gold standard in September 1931, the pressure developed into the so-called "liquidity crisis" described in last year's *Survey*.¹

¹ Pages 211-219.

Even during the earlier period of relatively moderate liquidation there had been a disquieting number of bank failures, and the panic period sharply accentuated this trend. By the end of 1932, over 10,000 banks of the 29,000 which had been in operation in 1922 had closed their doors, locking up deposits amounting to \$5,000 million. Half of these failures, it should be added, took place in the seven good years from 1922 to 1929, the remaining 5,000 in the three years of depression 1930-1932 — mostly in 1931. The mortality was greatest among the smaller banks which were not members of the Federal Reserve system. Over one-third of the failures took place in villages with a population of less than 500, and one-half in villages with less than 1,000 inhabitants.

Other factors placed a heavy strain upon the United States banking system in this period of panic. Gold and currency hoarding within the country, which first became marked towards the end of 1930 and was later reduced, became intensified again in the second half of 1931 after the United Kingdom had left the gold standard and there was some discussion of the United States following suit. It is estimated that, by the end of June 1932, the amount of currency hoarded in the United States was at least \$1,600 million.

At the same time, there were very considerable withdrawals of foreign short-term credit, reflected in large gold exports as well as a reduction of American short-term assets abroad. Various European banks strengthened their domestic position by withdrawing their short-term assets, principally from New York. Between the end of June 1931 and the end of June 1932, the total monetary gold stock of the United States declined by \$1,100 million.

It is obvious that such tremendous drains, not only upon the total deposits, but upon the reserves which are the heart of the whole credit system, involved further drastic deflation. The banks were forced to contract their advances, and, as the margins of security shrank, collateral holdings were thrown upon the markets, which declined precipitately. By the end of June 1932, commodity prices, security values, industrial production and employment had touched new low records for the depression and remained at levels lower than any experienced since the war. During the twelve months ending June 30th, 1932, the total loans and investments of the member banks were reduced by \$6,000 million, or 17 per cent as compared with 6 per cent in the preceding twenty-one months. Unlike the previous period, however, the deflation was not concentrated upon the ordinary commercial loans which were most immediately subject to banking pressure. In 1931-32, it was a deflation of security

loans, and therefore of security values, which was most marked. In the process, the investments made by the banks themselves were subjected to heavy losses, and it is estimated that, from June 1931 to June 1932, the losses sustained by American banks on their bond holdings amounted to at least \$2,000 million, or enough to wipe out half the paid-up capital of all American banks in existence at the former date.

After the breakdown of the gold standard in September 1931, a combination of difficulties — the strained condition of municipal finances, domestic hoarding, foreign credits subjected to standstill agreements, the withdrawal of short-term balances, together with further heavy falls in real-estate values and security prices — created great pressure upon the cash bases of bank credit. Emergency measures were put into operation by the Federal Reserve Banks and the Government in order to counteract the effect of this pressure. These measures took three principal forms. The Federal Reserve Banks in the early stages had greatly extended re-discounts to the member banks ; in February, however, they began once more to buy Government securities on a great scale in the open market and so to facilitate repayments of this indebtedness by the member banks. Between the end of February and the end of June 1932, the Federal Reserve Banks' holdings of United States Government securities rose from \$740 millions to \$1,784 millions.

In October 1931, the National Credit Corporation had been formed, on the initiative of President Hoover, by several large banks joining forces to extend credit to banks in temporary difficulties. While this measure appeared to assist in restoring confidence temporarily, there was a recrudescence of banking failures in December and January. In February 1932, therefore, the Reconstruction Finance Corporation was organised and took over the business of the National Credit Corporation. The capital stock of the Reconstruction Finance Corporation (\$500 million) was entirely paid up by the Government, which also purchased \$825 million of 3½ per cent notes from the corporation, raising the necessary funds by issuing its own bonds and Treasury bills, which were in turn largely taken up by the Federal Reserve Banks. With this capital in hand, the Reconstruction Finance Corporation made large advances principally to banks, trust companies, railways and insurance companies. The purpose of these loans, amounting to over a billion dollars at the end of June 1932 and to double that amount by the end of the year, was primarily to enable solvent institutions to survive the panic phase of the crisis.

The third line of defence against the panic was by legislation, notably the Glass-Steagall Act passed in March 1932, designed to

give greater powers to the Federal Reserve Banks in the creation of credit. The gold reserves are required partly as cover for the domestic note issue and partly against the risk of an external drain of gold. The demand for notes created by the hoarding that had developed and the gold exports necessitated by the withdrawal of foreign short-term balances had greatly reduced the amount of "free gold" over and above the statutory reserve requirements laid down by existing legislation. There was at that time ample gold to meet foreign obligations, but the open-market operations of the Federal Reserve Banks required a greater amount of "free gold". The Glass-Steagall Act authorised the Federal Reserve Banks to use Government securities, in addition to "eligible paper" and gold or gold certificates, as collateral for the note issue. In this way, the "free gold" holdings of the banks were greatly increased and a larger element of elasticity was introduced into the banking system.

In the same way, the bank-notes issued by the national banks were given a wider basis of cover by legislation allowing them to be issued against a greater number of specified Government securities, thus affording a considerable potential expansion of circulation. The Emergency Relief Act of July 1932 also extended the powers of Federal Reserve Banks to make advances, previously limited to member banks, to individuals and corporations under certain circumstances.

The combined effect of this legislation to give greater elasticity to the banking system, of the positive action by the Federal Reserve Banks to make credit cheaper and more abundant, and of the provision of Government loans through the Reconstruction Finance Corporation, together with the easing of the crisis in the United States and elsewhere, was to usher in a period of comparative tranquillity in the second half of 1932. The expansion of Federal Reserve credit, which, theoretically, might have been made the cash basis of an expansion of member-bank credit up to about \$10,000 million, was, in fact, used by the member banks to improve their liquidity. Of the \$1,000 million put into circulation by the Federal Reserve Banks' purchases of Government securities, about \$500 million actually found its way to the member banks, who used almost \$400 million to reduce their indebtedness, and the remaining \$100 million to increase their balances, with the Reserve Banks. There was, by the end of 1932, no expansion of member-bank credit; but the previous deflation was brought to an end and the number of bank failures decreased very considerably.

Towards the end of the year, however, despite the persistence of monetary ease, bank failures began to increase, and, as the

autumn revival gave way to recession, a wave of mistrust marked by withdrawals of deposits, and very soon by actual currency and even gold hoarding, led to runs, first upon particular banks and then upon banks in general in many widely separated parts of the country. The panic that ensued was the most spectacular breakdown of public confidence witnessed in any country for many years. In the middle of February, there were runs on important banks in the State of Michigan, and all banks in the State were closed for a week. In other parts of the country, confidence failed rapidly, and it was a matter only of days before similar runs and banking holidays had occurred in every State. On March 4th, the day of his accession to power, President Roosevelt, faced with banking holidays in every State and the closing of the New York and other stock exchanges, declared a national banking moratorium.

Some indication of the strain on the banks may be gleaned from the fact that, between February 1st and March 8th, the monetary circulation increased from \$5,652 million to \$7,538 million, no less than \$455 million of the increase taking place on one day, March 3rd. The drain began in the interior; but the country banks drew heavily on their New York correspondents as well as on the Federal Reserve Banks. The New York City banks in six weeks mobilised over \$1,300 million, which they placed at the disposal of their depositors and correspondents. The Federal Reserve Banks in the same period discounted \$1,145 million of new bills and bought acceptances to the extent of \$384 million, besides increasing their holdings of Government securities by \$117 million. The gold holdings of the Treasury and the Federal Reserve Banks also dropped by \$600 million, at least half of which was hoarded. The reserves of the Federal Reserve Banks, despite the legislation described above, were again brought down, by gold export and hoarding, dangerously near the minimum reserve ratio. The ratio of the New York Bank fell to 41.4 per cent, and it was kept above the legal minimum of 40 per cent only by selling Government securities to, and re-discounting the Bank's own paper with, other Federal Reserve Banks. The ratio for all the Federal Reserve Banks fell to 45.1 per cent.

The President, having on March 4th proclaimed a national bank holiday, summoned Congress to meet on March 10th, meantime imposing an embargo upon the export of gold and silver. Two days later the Federal Reserve Banks were instructed to pay out no more gold or gold certificates and to prepare lists of gold hoarders. Congress, at its special session, approved emergency measures giving the President complete control over all banks, authorising the re-opening of banks declared to be sound

and the re-organisation of others. The Federal Reserve Act was amended so as to give greater powers both in regard to note issues and in regard to advances.

On March 13th, some banks were allowed to re-open, and, by the end of March, 12,800 out of a total of some 17,000 were in full operation once more. The sound banks had controlled well over 90 per cent of deposits, and there was in consequence a rapid liquidation of the immediate crisis. Currency flowed back to the banks, which were enabled to repay their indebtedness and increase their balances with the Reserve Banks. The improvement is well illustrated by the following table :

United States Monetary and Credit Movements, March 8th to August 9th, 1933.

\$(000,000's)

Date	Money in circulation	Federal Reserve credit outstanding				Member-bank reserve balances
		Bills discounted	Bills bought	United States Government securities	Total	
March 8th	7,538	1,414	417	1,881	3,712	1,776
15th	7,269	1,232	403	1,899	3,534	1,964
29th	6,353	545	310	1,838	2,693	1,987
April 12th	6,147	428	247	1,837	2,512	2,096
26th	5,994	385	177	1,837	2,399	2,136
May 10th	5,892	338	113	1,837	2,288	2,089
24th	5,795	312	43	1,862	2,217	2,194
June 7th	5,767	277	11	1,912	2,200	2,204
21st	5,696	222	9	1,955	2,186	2,205
July 5th	5,752	182	26	1,995	2,206	2,219
19th	5,635	163	10	2,017	2,190	2,289
August 9th	5,608	156	8	2,048	2,212	2,376

The struggle for liquidity in the days preceding the crisis and the locking up of deposits in the banks which remained closed had naturally exerted a deflationary effect, and it was not till after the abandonment of the gold standard on April 19th that a definite upward movement took place in loans and investments. The subsequent developments are discussed in Chapter XI.

On June 16th, the Banking Act, 1933, was signed. A Federal Deposit Insurance Corporation was set up in order to guarantee deposit accounts. Greater powers were given to the Federal Reserve Banks to control speculative operations by member banks ; security affiliates are required to be separated from the banks and more definite separation of deposit and investment banking is demanded ; branch banking within States is facilitated,

and the regulations governing demand and time deposits are tightened considerably. In addition, the payment of interest upon demand deposits was prohibited. In the following week, ending June 21st, net demand deposits in ninety leading cities decreased by \$384 million, while time deposits rose only by \$73 million. The deposits withdrawn appear to have been utilised largely in the purchase of industrial and other interest-earning securities, a development which transferred a considerable amount of such securities from bank portfolios to private ownership.¹

THE DEVELOPING FUNCTIONS OF CENTRAL BANKS.

The special position of Central Banks in the economic life of modern communities is derived from their double relationship, on the one hand, to the State, in respect of monetary policy, and, on the other, to the commercial banks, and, through them to the industrial and trading community, in respect of the supply of credit. The origins of particular Central Banks may be traced to different combinations of circumstances — the necessities of public finance, a desire to foster financial or industrial development, or the desirability of establishing sound currency policies. Whatever these origins may have been, central banking practice has steadily evolved towards very similar responsibilities and purposes in every modern country. Methods of achieving those purposes vary, and the authority of the Central Bank is greater in some countries than in others ; but there is a continuous development of function and a growing tendency towards co-operation among the various Central Banks. While it is possible to exaggerate the extent to which these developments have proceeded, and, in particular, to attribute to the Central Banks powers and possibilities of action which they have not yet achieved, the spread of central banking and the development of central banking practice are among the most significant advances in social organisation that have sprung from the stress of recent years. It is characteristic of the modern spirit also that these institutions, while for the most part private or at least politically independent in their organisation, act as a bridge between the individual initiative which dominates the economic system and the public responsibilities of Governments. In so doing, they necessarily endeavour to combine the freedom characteristic of private enterprise with a sense of public responsibility.

The pervasive importance of credit in modern economic organisation renders the function of Central Banks one of peculiar

¹ *The Annalist*, July 7th, 1933, pages 4-5.

delicacy and significance. In simpler times, the State prerogative and duty of providing stable and adequate means of exchange was less closely linked than at present with the conduct of industry and trade upon a credit basis. Coinage and the issue, or at least the regulation, of currency remains a prerogative of the State ; but, except in abnormal circumstances, coins and currency issues do not govern, but are rather governed by, the volume of credit in use. The commercial banks act as the channels through which credit is accumulated and distributed, and the function of the Central Bank in this respect is to act as a bankers' bank.

This means, in practice, that the main responsibility of Central Banks is that of maintaining, not only national, but international economic equilibrium. It is obvious that Central Banks do not have, nor is it likely that they will ever have, the power to govern and direct all the factors that enter into these equations. In the balancing of the forces which affect national and international economic equilibrium, Governments, Central Banks, commercial banks and private individuals all have a rôle to play. It is, indeed, essential for progress that as much freedom of initiative as is compatible with orderly development shall be preserved. It is, therefore, not a question of Central Banks developing into economic super-governments ; but rather of their discharging an essential mediatory and regulatory function in the economic organisation. Any governing action they perform resembles that of the "governor" which absorbs irregular stimuli and smooths out the rhythm of an engine. If the stimuli are too irregular, they may become uncontrollable.

It follows that, in the pursuance of international co-operation, the Central Banks have eschewed any notion of creating an international Central Bank of Central Banks in the sense of a controlling and supervising institution. The essential problems of international economics, it is argued in a later chapter, are problems of balancing the activities and relations of a series of independent, but related, national economies. The Central Banks, through their common organ of consultation, the Bank for International Settlements, can and do contribute towards the measures necessary to harmonise national economic policies in the common international interest ; but they do so by consultative co-operation rather than by unified action.

The progress made in pursuing the policy of cheap credit, initiated, in its most recent phase, by the lowering of the Bank of England's discount rate from 6 to 5 per cent in February 1932, illustrates the principles sketched above. The widespread and practically continuous lowering of Central Bank discount rates since that time is summarised in the following table.

Rates of Discount of Central Banks. ¹ (End of month.)

Country	1931	1932				1933	
	XII	III	VI	IX	XII	III	VI
South Africa	6	6	6	6	5	4	3.5
Germany	7	6	5	4	4	4	4
Austria	8	7	7	6	6	5	5
Denmark	6	5	4	4	3.5	3.5	3
United States ²	3.5	3	2.5	2.5	2.5	3.5	2.5
France	2.5	2.5	2.5	2.5	2.5	2.5	2.5
Greece	11	11	11	10	9	9	7.5
Hungary	8	7	6	5	4.5	4.5	4.5
India	8	6	5	4	4	3.5	3.5
Italy	7	6	5	5	5	4	4
Japan	6.57	5.84	5.11	4.38	4.38	4.38	4.38
Norway	6	5	4.5	4	4	4	3.5
The Netherlands	3	3	2.5	2.5	2.5	2.5	4.5
Poland	7.5	7.5	7.5	7.5	6	6	6
Portugal	7	7	6.5	6.5	6.5	6	6
Roumania	8	7	7	7	7	7	6
United Kingdom	6	3.5	2	2	2	2	2
Sweden	6	5	4	3.5	3.5	3.5	3
Switzerland	2	2	2	2	2	2	2
Czechoslovakia	6	6	5	4.5	4.5	3.5	3.5
Turkey . . . . .	.	8	8	7	7	5.5	5.5

The reduction of Central Bank rates spread quickly to the money markets, which in turn lowered the rates at which they were prepared to advance credit to short-term borrowers. These market rates of discount, in fact, fell to extraordinarily low levels, indicating an abundance of credit but a dearth of borrowers in certain countries. The extent of the fall in market rates is revealed in the following table :

Market Rates of Discount. ³ (Monthly average.)

Country	1931	1932				1933	
	XII	III	VI	IX	XII	III	VI
Germany	7.32	6.09	4.75	4.25	3.88	3.88	3.88
United States :							
(a)	3.88	3.83	2.94	2.25	1.64	3.00	1.75
(b)	3.00	2.50	0.88	0.75	0.38	2.88	0.38
France	1.88	1.73	1.12	1.06	1.06	2.13	1.85
The Netherlands	1.47	1.21	0.52	0.38	0.38	0.69	2.19
United Kingdom	5.88	2.59	1.06	0.66	1.09	0.63	0.50
Switzerland	1.75	1.50	1.50	1.50	1.50	1.50	1.50

(a) Commercial paper. (b) Bankers' acceptances.

¹ *Monthly Bulletin of Statistics.* * Federal Reserve Bank of New York.
² *Monthly Bulletin of Statistics*, No. 8, 1933.

While it is thus evident that short-term credit was extremely plentiful and cheap in the principal money markets, there were many obstacles which prevented this cheap credit from penetrating quickly into the industry and trade of the countries concerned. Long-term interest rates upon both public and private investments remained difficult to reduce. But the most serious difficulties lay in the frozen assets and investment losses of the banks themselves and in the necessity for carrying through very considerable reconstructions of industrial capitalisation. In other words, some house-cleaning was necessary before the cheap credit policy could become effective. The debris left by the financial panic had to be cleared away before any considerable revival of economic activity could be looked for.

The cheap credit policy, however, was not ineffective. In the first place, as has been stated above, it enabled the commercial banks to improve their own cash position and so enabled them to face with greater assurance the difficult problems of industrial reconstruction. More favourably situated borrowers, moreover, were able to take advantage of the lower rates ruling in the short-term market and many Governments followed the lead given by the United Kingdom at the end of June 1932 in launching large schemes of long-term debt conversion. The Australian, Belgian, Danish, Dutch, French, Italian, New Zealand, Swedish and Swiss Governments all converted part of their public debt. Opinions differ as to whether particular Governments have made the fullest use of these conversion opportunities; but the total effect has been, not only a considerable relief to the budgets, but also a strong downward impetus to long-term interest rates. Some industrial enterprises also were able to convert part of their debenture obligations, and there are indications that the conversions and consolidations of public debt have by no means been completed at the moment of writing in July 1933.

The downward movement of interest rates thus initiated was followed during the latter half of 1932 by reductions of rates by savings banks, building societies and similar institutions. In many countries, notably Austria, Czechoslovakia, Finland, Italy and Sweden, the Central Banks intervened in order to secure a more uniform adjustment than would result from purely individual action. In several countries, also, Government initiative was taken to effect a reduction of the interest rates charged by commercial banks. This was notably the case in Italy, Poland and Denmark.

Positive action by the Central Banks, either individually in their own countries, or collectively by the stronger Central Banks through the medium, and with the co-operation of, the

Bank for International Settlements taking steps to relieve the pressure upon Central Banks in other countries, has gone some distance towards freeing the commercial banking systems from the obstacles which prevented them from passing on the reduction of interest rates to industrial enterprises.

Central Bank action was particularly effective in the reduction of the frozen short-term indebtedness which was a serious obstacle to the freeing of international financial and economic relations. The Bank for International Settlements, in its second annual report, estimated the total amount of short-term international indebtedness which existed at the beginning of 1931 as more than \$10,000 million.¹ Later information leads to the belief that the full total was probably between \$12,000 and \$13,000 million. Of this large amount, almost half (about \$6,000 million) was liquidated during 1931 either by repayment or by writing off losses. The process of liquidation was facilitated by emergency help made available by Central Banks, by the Bank for International Settlements, by the principal capital centres and by Treasuries. The total of such emergency grants has been estimated at about \$1,000 million.² If allowance is made for these new obligations, the total outstanding foreign short-term indebtedness at the beginning of 1932 was about \$7,000-8,000 million. Repayments continued throughout 1932, and by the end of the year the total had probably been reduced to some \$6,000 million.³

While grave financial problems still confront the world, nationally and internationally, and progress in solving them is necessarily slow and difficult, enough has been said to indicate that there has been progress. It is obvious that the unusual stress of recent years has both tested the capacities and developed the functions of Central Banks and, in particular, has fostered a degree of co-operation among them that is new at least in its continuity. As an illustration of the developing functions of many Central Banks may be cited the use of open-market operations, for example, by the Scandinavian banks. The outstanding feature of the co-operation that is developing among Central Banks is the rôle played by the Bank for International Settlements.

It is significant that successive expert recommendations by the Gold Delegation, the Preparatory Commission of Experts

¹ Bank for International Settlements, "Second Annual Report", May 1932, page 11.

² *Idem*, page 12.

³ Bank for International Settlements, "Third Annual Report" May 1933, page 11.

and the Sub-Committee on Technical Monetary Problems of the Monetary and Economic Conference have repeated and extended the pronouncements of previous international conferences by stressing the desirability of creating Central Banks in adequately developed countries where they do not now exist, and of fostering close and continuous co-operation between the central banking institutions of various countries. The evolution of central banking practice is one of the most important aspects of the re-organisation of financial machinery now in progress.

Chapter IX.

A WORLD IN DEBT.

A GENERAL PROBLEM.

The previous chapters of this *Survey* have described successively the contraction of prices, production, wages, profits, Government revenues, international trade and banking resources. In real goods and services, as well as in monetary values, there has been a progressive shrinkage of economic activity in practically every direction. Private individuals, business enterprises and national Governments are all faced with shrunken incomes and the world as a whole with broken organisation.

In these circumstances, the burdens of indebtedness, in some cases oppressively heavy even before the depression began, have not only become more burdensome, but have developed into awkward and obstructive causes of further deterioration in the economic situation. Illustrations of this fact are so obvious that they need not be multiplied. Heavy external indebtedness, forcing the agricultural countries to restrict their imports and maximise their exports, was a large factor in causing prices to fall. Over-indebtedness, both in agriculture and in manufacturing industry, has crushed profits between falling prices on the one hand and high overhead costs on the other. Debt charges are a principal cause of the budgetary strain that afflicts almost all Governments. The difficulty of transferring debt service from one national currency to another has not only aggravated monetary disorganisation, but has been a prime factor in creating the restrictions that have been imposed on international trade.

It is not intended in the present chapter to discuss the extent to which debt payments of any kind, national or international, governmental or private, were responsible for the financial crisis. That they played a large part, in the circumstances of the period before 1929, in making difficult the maintenance of a

flexible economic and financial organisation is generally admitted. In the previous *Survey* and in other documents, such as the report of the Gold Delegation, attention has been drawn to various aspects of their influence in straining the international financial mechanism and precipitating the crisis in 1929. The purpose of the present chapter is primarily to call attention to the magnitude and complexity of the problems now presented by the existence of such a large volume of indebtedness as was built up before 1929.

While there have been reductions of indebtedness in various directions, particularly among private persons and institutions, other forms, especially of Government debt, have proved difficult to reduce and have in many cases even been increased. This is one of the factors which make for greater inflexibility of economic organisation in such a period as the present. When, for any reason, fluctuations of business activity bring about a general shrinkage of incomes, the debts of Governments, partly because they are so largely on long term, are more difficult to reduce than those of private persons. The great extent to which Government activities increased during the war and post-war period, therefore, and the enormous growth of public indebtedness, aggravated the inflexibility of the economic system. The growth of large-scale business enterprises, in so far as it was financed by debt rather than by equities, worked in the same direction. Not only was the total of debt greater, but it was much more difficult to reduce by the elimination or re-organisation of unsound enterprises. Moreover, the strain on the public finances has caused an increase in the public debt of many countries.

The total nominal value of debt obligations, therefore, has, on the whole, been very little reduced during the depression, but has been maintained at levels which have become excessively burdensome as economic activity has contracted. The current service of these obligations to provide for interest and amortisation represents a much heavier proportion of the resources available to debtors. Even when amortisation payments are reduced or suspended and rates of interest are reduced by agreement or conversion, debt service in most countries and in most enterprises absorbs a much greater share of current income than was contemplated when the debts were contracted. The economic structure of the world has shrunk so greatly and it has proved so difficult to reduce the financial obligations undertaken in more prosperous years that the gap between economic possibilities and financial necessities has become a dominating problem of world economics.

The conflict of economic and monetary theories that has run through all discussions of the depression from every angle reaches

its culmination at this point. There are two main schools of thought, the one insisting that economic activity should be "reflated", primarily by monetary action to raise prices, so that debt burdens may again become tolerable; the other maintaining that no permanent recovery of economic activity is possible until debts have been written down, not necessarily to the low levels of paying capacity set by the diminished economic activity prevailing at the lowest point of the depression, but at any rate to levels lower than those ruling when the debts were originally contracted. There are many aspects of this conflict of opinion, both theoretical and practical, and the extreme positions on either side tend to yield place to compromise solutions combining some measures of debt reduction with proposals to raise prices and restart economic activity. The conflict of opinion is still important, however, in regard to priorities and methods of solution. Whether debt adjustment is to precede or follow economic improvement and how to proceed in either direction remains a subject of lively controversy both nationally and internationally. The main cleavage on methods of stimulating economic recovery is between those who maintain that such recovery can come only by freeing trade and industry from the excessive restrictions that have been imposed upon them in recent years and those who believe that monetary action can raise price-levels and stimulate economic activity even in present circumstances.

It is not intended here to attempt the impossible task of endeavouring to describe the total debt situation of individual countries. The circumstances differ so greatly from country to country that the situation in each must be the subject of separate examination, which is best made by national experts. One or two examples may perhaps be given to illustrate the fact that, in addition to the problems of international indebtedness which are the main subject of this chapter, domestic debt constitutes a very important and pressing problem almost everywhere.

Estimates of the total of indebtedness varying in completeness are available for a number of countries, but there are great statistical difficulties presented in any attempt to make such estimates precise and avoid double counting. Six recent estimates for the United States by recognised statisticians vary from \$155,000 million to \$234,000 million.¹

In Germany, total indebtedness was estimated to amount, at June 30th, 1932, to RM. 91,500 million. This total long- and short-term indebtedness, which omits debts owed within

¹ Cf. *National Industrial Conference Board Bulletin*, February 20th, 1933.

the main economic groups distinguished below, was distributed in the following way :

*Indebtedness of German Economic Groups.*¹

Economic debtor group	Indebtedness June 30th, 1932	Interest according to rates ruling at the end of 1932.
	RM. (000,000's)	
Industry and trade	27,360	1,790
Agriculture ²	10,650	560
Housing ³	23,200	1,170
Public authorities	30,250	1,690
Total	91,460	5,210

Similar estimates are not available for earlier years, but the following table, which shows the number of obligations outstanding,³ gives some evidence of the growth of the indebtedness to the end of 1931 and its stability thereafter :

Date	Obligations outstanding RM. (000,000,000's)
March 31st, 1928	20,968
December 31st, 1929	26,856
December 31st, 1930	30,483
December 31st, 1931	31,317
March 31st, 1932	30,567

The variety and complexity of indebtedness demands careful and detailed investigation in each particular case in the light of the special circumstances of the country concerned ; but the illustrations given above are sufficient to disclose the magnitude of the general problem. Not only national, but municipal and private debt, on long and on short term, held within the country and abroad, must be compared with the shrinkage of national incomes. There are certain developments common to most countries — the general tendency examined in Chapter V for industrial and agricultural debt to increase before the depression, the growth of public debt resulting from the war, and the budgetary strain since the depression, together with a widespread expansion of local government services reflected in increased municipal debt.

¹ *Wirtschaft und Statistik*, 1. Mai and 1. Juni Hefte, 1933.

² Debt to creditors within the same group was, in the case of agriculture, RM. 1,200 million, and housing, RM. 4,200 million.

³ Of these, RM. 63 milliard are long-term debt.

INTERNATIONAL DEBTS AND INTERNATIONAL ECONOMIC EQUILIBRIUM.

The international, as distinct from the national, aspects of the greatly increased indebtedness which weighed upon the post-war world present a series of problems which demand further consideration. The difficulties that arose in transferring from one national economy to another the payments due on account of foreign debt cannot be considered wholly apart from the distributive conflict referred to in the preceding section ; but they are sufficiently serious in themselves to warrant careful examination. It may well happen, for example, that the main representatives of creditors in an important lending country may be in sharp conflict with other important groups whose interests lie in the stimulation of domestic trade and its protection from imports. Different classes of creditors, particularly those to whom public debts and private commercial debts respectively are owed, may also be in conflict concerning priorities of claims. In such circumstances, when group interests conflict within a country, it becomes difficult to estimate the national interest as a whole or to determine national policy. No attempt is made here, however, to make an estimate of these situations, other than to point out certain elementary and generally agreed conclusions concerning the effects of such conflicts of group interests, and the policies resulting from them, upon the conduct of international economic relations in general.

The main consideration to be borne in mind is that put forward in the previous *Survey* where attention was drawn to the predominantly national organisation of economic production and trade as distinct from the more international and even cosmopolitan organisation of finance. In the next chapter, it is argued that modern economic problems must be considered neither as purely national nor as cosmopolitan, but as arising in a series of national economies which are in shifting equilibrium one with another. The maintenance of international equilibrium through the interaction of the national price-systems (including such important prices as wages and interest-rates) was reasonably effective in the pre-war period when the gold standard provided a common measure of value. The dominance of the London money market enabled it to act as a reservoir and distributing centre of credit, while under a free-trade policy the English market served as an *entrepôt* for international commerce. The relative flexibility of the economic system facilitated the necessary adjustments of national price systems. In this period, great changes took place in the economic organisation of the world, and, in particular, large amounts of capital were transferred from the older industrial

countries to open up and develop first the interior plains of North America and later the South American agricultural countries, the British dominions in the southern hemisphere, and certain Far-Eastern countries. The magnitude of the price changes and therefore of the re-arrangement of production caused, for example, by the opening up of the American wheat lands, the introduction of refrigeration, the development of the South African goldfields, and the rapid rise of Japan as an industrial Power, was half-concealed by the smoothness with which international equilibrium was adjusted through the operation of the pre-war gold standard.

In the post-war period a great many complicating factors were introduced. Among them must be reckoned the rapid expansion of international indebtedness, the effective discharge of which demanded, not only an augmented volume of international commodity trade, but considerable shifts in the relations between national price systems. There arose, however, very great difficulties in adapting either national price levels or national economic organisation to the changed structure of international finance. Balances of payments could not easily be changed from passive to active in the case of debtor countries, or from active to passive in the case of countries whose creditor position had created the necessity of receiving an increased volume of imports in discharge of debt. Such transformations would have required very radical changes in national economic organisation at a time when such organisation was less flexible than it had been before the war.

The true difficulties of this situation were not revealed while a large number of the currencies, particularly of debtor countries, remained independent, exchanges fluctuated, and inter-governmental debt payments were not settled. As one currency after another returned to the gold standard and exchange parities once more became fixed, while successive debt settlements were arranged, the strain upon the newly restored mechanism for maintaining international financial equilibrium became greater. For a few years between 1925 and 1929 the payment of international financial obligations was rendered possible without drastic re-arrangement of national economies by the free flow of new capital exports, largely from the United States, to the debtor countries. When this export of capital began to fail in 1928-29, the pressure on the balances of payments of the debtor countries depressed prices, the credit expansion broke and the strain of international adjustment finally caused the collapse of the international monetary mechanism.

When this development occurred, the full complexity of the problems involved in the maintenance of international economic

and financial equilibrium were revealed by the variety of forces which it was necessary to consider in any proposals once more to stabilise the exchange ratios between different currencies. Not only technical monetary problems, such as the use of gold in the monetary systems, credit policies, reserve ratios and interest rates, but more general economic considerations, such as the effect of different exchange ratios upon export industries, as well as upon domestic price levels, and therefore upon wages and production costs, became a matter of serious concern.

In face of such complicated problems, there was a general retreat from international economic co-operation, and measures of national economic defence were hurriedly improvised to protect national industries and standards from international competition. The aggregate effect of these measures was still further to restrict economic activity and depress prices, particularly in those commodities exchanged between national economic systems, so that the discharge of international financial obligations became still more difficult. The volume of international debt obligations, which was too great for international trade to carry except when lending was pursued as freely as it was between 1925 and 1929, was still more difficult to discharge in 1932, when lending had virtually ceased and international trade had fallen to little more than one-third of its value in 1929.

It was not long, therefore, before exceptional measures had to be taken to deal with the debt service, which could no longer be met either by the export of goods or by the contraction of new loans. The moratorium proposed by President Hoover in June 1930 for the suspension of inter-governmental debt and reparation payments for one year was only the beginning of a long series of measures, which were quickly extended to private as well as public international debts. The remainder of this chapter gives in broad outline a summary of the principal measures adopted ; but it is being written *in medias res* before any general or permanent solutions have been found and while temporary arrangements in particularly acute cases are all that can be recorded.

INTER-GOVERNMENTAL INDEBTEDNESS.

The inter-governmental indebtedness arising from the war of 1914-1918 has been the subject of numerous official conferences and diplomatic exchanges during the last fifteen years. The official and unofficial publications both on reparation payments and on war debts form a voluminous literature to which it is

unnecessary to add much here.¹ Both politically and economically, the existence of these large inter-governmental obligations consequent upon war expenditures were a very disturbing factor in the post-war years. Successive settlements and revisions, both of war debts and of reparation payments, occupy a large place in the diplomatic history of the first post-war decade; but the full economic effect of such arrangements was not revealed until international lending began to diminish rapidly in the months before the New York Stock Exchange crisis precipitated the depression in the latter part of 1929.

While historically and legally separate, payments on account of war debts and of reparations present economic problems largely similar in character, and as early as June 1931 were linked together by official action in which the initiative was taken by the principal creditor Government. The moratorium proposed at that time by President Hoover applied to both sets of payments. It is not intended here to examine the earlier history of either question, or to analyse the extent to which the payments actually made up to the end of June 1931 were responsible for the derangement of international trade and finance that lay behind the depression. It may be pointed out, however, that successive debt settlements after 1923 and the reparation (Dawes) agreement in 1924 provided for payments on inter-governmental account during the years when the international monetary system was being restored by the return of one country after another to the gold standard. At the same time as an effort was made to re-establish the mechanism by the utilisation of which national economies had been kept in equilibrium, that mechanism was loaded with the additional burden of transferring from one currency to another exceptionally large amounts for which there were no offsetting commodity transactions. As long as credit remained good and international loans were freely extended, these payments were transferred, though it has been maintained that such transferences were among the causes which led to excessive strain on the monetary systems. There were no important revisions of the debt settlements; but in 1929 the Young plan was worked out as a substitute for the 1924 settlement of reparation payments. Before the Hague agreements in 1930 supplemented the Young plan, however, the depression had begun. Not only had international lending shrunk greatly, but prices had fallen and the quantum of international trade also had

¹ Cf., e.g., among recent works, Denys P. Myers, "The Reparations Problem", Boston World Peace Foundation, 1930; John W. Wheeler-Bennett, "The Wreck of Reparations", London, Allen and Unwin, 1933; and Harold G. Moulton and Leo Pasvolksy, "War Debts and World Prosperity", Washington, The Brookings Institution, 1932. A convenient short historical summary of the war debts is contained in "The War Debts", Supplement to *The Economist*, London, November 12th, 1932.

been reduced, so that the possibilities of transferring large sums on inter-governmental account were much diminished. Payments were continued, however, until threatened financial collapse in Germany led to the Hoover moratorium in June 1931.

The large sums affected by the moratorium were given in the preceding *Survey*.¹ For the year ending June 30th, 1932, the United States suspended net receipts amounting to £53,600,000; France (£16,100,000) and the United Kingdom (£9,700,000) were the principal other net creditors to forgo payment in that year, while Germany, as the chief debtor, was relieved to the extent of £77,000,000. Several of the smaller countries were greatly affected also by the moratorium, Yugoslavia, for example, losing net receipts to the value of £3,300,000, while Australia and New Zealand were relieved to the extent of £3,100,000 and £1,420,000 respectively. The moratorium was not renewed when it expired at the end of June 1932, and the problems of reparation payments and war debts had therefore to be dealt with separately as before.

Brief reference was made in the preceding *Survey* to the investigations into and developments of the reparation problem that took place during 1931-32, while the Hoover moratorium was in force.² Following the London Conference (July 29th to 23rd, 1931), the Bank for International Settlements set up a Committee of experts to enquire into the financial position of Germany. This Committee met at Basle on August 8th. A Creditors' Committee also met from August 14th to 19th and arranged the first standstill agreement on private commercial debt. For a time, the situation seemed to improve in Germany; but after the abandonment of the gold standard by the United Kingdom in September, renewed weakness was evident, and, on November 19th, the German Government asked the Bank for International Settlements to convene the Consultative Committee provided for under the Young plan. This Committee met at Basle on December 7th, and reported that, after the expiration of the Hoover moratorium, Germany would not be able to resume payment of the conditional annuities. In February, the standstill agreement on private commercial debt was renewed.

The next stage of development was the convocation of the Lausanne Conference on June 16th, 1932. The final agreement reached at Lausanne has already been summarised in Chapter I. The agreement, by an understanding secretly reached during the Conference but revealed shortly afterwards, was not to "come into final effect until after ratification"; but it was made clear by a declaration of the President at the plenary session on July 8th that, "in the event of any inability to fulfil this agreement

¹ Pages 256-7.

² League of Nations *World Economic Survey*, 1931-32, pages 70-82 and 307-8.

and its annexes, a further conference will be held". No further development occurred up to the time of writing (July 1933), and the situation in regard to reparation payments therefore remains as it was left at Lausanne. No further payments have been made; but the agreement has not been ratified and has not therefore come into final effect.

Interest during 1932 and 1933 shifted to the Inter-allied debt problem. The first payments after the Hoover moratorium expired fell due on December 15th, 1932. Most of the debt settlement agreements contained provisions for postponement of capital payments for limited periods¹; but the ninety days' notice necessary for such postponement was not given in September. In early November, the presidential election was held in the United States and shortly afterwards the United Kingdom, followed by the other debtor Governments, began an exchange of notes with the United States Government. This exchange included an exposition of the case for cancellation on general grounds of world prosperity contained in the British note of December 1st.² The situation was complicated by the fact that the new President did not take office till March 1933 and also by a joint resolution passed by Congress on December 22nd, 1931, when ratifying the Hoover moratorium, declaring that it was "against the policy of Congress that any of the indebtedness of foreign countries to the United States should be cancelled or reduced".

The date of payment, December 15th, arrived without any agreement being reached, whereupon the United Kingdom Government paid its obligation (the largest due at that date) in full by transferring gold to the value of \$95,500,000 purchased from the Bank of England, at the same time making a unilateral declaration that such payment was to be regarded as an instalment in view of a final settlement. Italy, Czechoslovakia, Finland, Greece, Latvia, Lithuania, Roumania and Yugoslavia also paid their instalments; but no payment was made by France, Poland, Belgium, Estonia and Hungary.

This was the situation when, in April 1933, the President of the United States invited representatives from the principal countries concerned to participate in personal conversations at Washington. The scope of these conversations, which were conducted individually and covered, not only war debts, but other economic and political questions, was extended to other countries than those concerned with war debts. The discussions were secret, but successive official *communiqués* indicated the general nature of the subjects discussed, which included the convocation of the Monetary and Economic Conference for June 12th, and disarmament.

¹ Cf. *Economist*, loc. cit., page 6.

² Cmd. 4210 (1932).

As the date of the next payment (June 15th) drew near, it became clear that no agreement had been reached upon war debts and the Conference opened in London without any decision on this question. After secret negotiations, however, the Chancellor of the Exchequer announced, on June 14th, a compromise arrangement by which a token payment was made on account of the British instalment. The British telegram of June 13th repeated the declaration made in December that payment was not regarded as a resumption of the annual payments but "as a capital payment of which account should be taken in any final settlement". The sum paid was \$10 million in lieu of the amount due (\$75,950,000), and payment was made in silver at the rate of 50 cents per ounce in virtue of a provision in the Farm Relief Act, signed on May 12th, 1933. The necessary silver for the payment was purchased from the Indian Government. As the current market price of silver was 36 cents per ounce, the actual sterling cost of the payment was £1,156,000.¹ The President of the United States, in acknowledging receipt of this token payment, intimated that he had "no personal hesitation in saying that I do not characterise the resultant situation as a default".¹

Of the other debtor countries, Finland paid its instalment in full, Italy, Czechoslovakia and Latvia followed the British lead in making a token payment, while the other countries did not pay. The amounts due and the payments made on June 15th, 1933, are shown in the following table :

Country	Full amount due \$	Amount paid \$
United Kingdom ²	75,950,000	10,000,000
Italy ²	13,545,437	1,000,000
Czechoslovakia	1,500,000	180,000
Finland	148,592	148,592
Latvia	119,609	6,000
Roumania ³	1,000,000	29,100
France	40,738,567	—
Belgium	6,325,000	—
Poland	2,953,362	—
Estonia	228,182	—
Hungary	32,025	—
Lithuania	123,535	—
Yugoslavia	275,000	—
Greece ⁴	150,000	—

¹ Cf. *London Times*, June 15th, 1933.

² Payments made in silver.

³ Roumania later paid \$25,000.

⁴ Due on July 1st.

In the meantime, the payments due to the United Kingdom from the Allies and certain Dominions were not demanded either in December 1932 or June 1933. When it became known that the United Kingdom would pay the December instalment of its debt to the United States, the New Zealand Government formally offered to pay its instalment to the United Kingdom, but the latter preferred not to accept it.

At the time of writing (July 1933), no further developments have occurred, and negotiations have not begun either in respect of the next instalment due on December 15th, 1933, or of a final settlement.

THE MAGNITUDE OF INTERNATIONAL INDEBTEDNESS.

Attempts to estimate totals of world international indebtedness meet with a great many statistical difficulties. In spite of considerable progress in recent years, national statistics are still very incomplete, and only a few countries possess complete census figures of foreign indebtedness. Generally, the estimates are based on capital issues and redemptions and are liable to a considerable margin of error. In some countries, it is the market value of the claims, but in most countries, including many of the most important, it is the nominal value which is given. Fixed property and shares are generally included in the estimates in such a way that exclusion is impossible without recourse to the original data in each case.

The most complete collection of co-ordinated statistics concerning international debts and claims of individual countries, and the interest payments on such debts and claims, is available in the League of Nations *Balances of Payments, 1930*,¹ and *Balances of Payments, 1931-32*.² On the basis of the information given in these publications as to the foreign claims of twenty-four countries and estimates of the situation in the remaining countries, the total gross international indebtedness of all countries on account of fixed-interest securities, but excluding direct industrial investment, on both short and long term, at the end of 1932, may perhaps be roughly estimated at a nominal value of about \$35,000,000,000.³

¹ Geneva, 1932.

² The present text incorporates some information from the 1931-32 volume, which will shortly be published.

³ The most important creditors are the United Kingdom (which is creditor for about 25 per cent of the above figure), the United States (22 per cent), France (above 10 per cent), Switzerland and Netherlands (5 per cent each), Germany, Canada, Belgium, Japan, Sweden, Czechoslovakia and Spain.

The political debts, which, according to the German Institut für Konjunkturforschung,¹ had, after the Lausanne agreement, a present value of gold \$9,000,000,000, are not included in the above figure.²

The main and almost the only utility of this estimate, and those quoted in the footnote below, lies in demonstrating the magnitude of the capital obligations expressed in terms of moneys that have greatly appreciated in value.

The annual interest and amortisation payments due on the total world international debt may be conservatively estimated at \$2,000 to \$2,500 million. It is difficult to estimate any more precise figure on account of the considerable and growing repatriation of the external bond issues of many countries, against which must be set sales of domestic issues to foreign buyers. This is a large amount to be transferred between national currencies. The impossibility of payment in any other way than by goods is obvious from the fact that the amount is about 20 per cent of the world's monetary gold stocks, and more than the total monetary gold stocks of all debtor countries. It is significant, on the other hand, to observe that the value of the import trade of the world has fallen from gold \$35,600 million in 1929 to only \$13,900 million in 1932.

¹ *Wochenbericht des Instituts für Konjunkturforschung*. The present value of all future annuities was calculated on the assumption of an interest rate of 5 per cent. From this amount the debt of Russia is excluded.

² The German Institut für Konjunkturforschung (*Wochenbericht*, 1932-33, page 215) has estimated the total international indebtedness (including political debts) as RM. 200,000 million (gold \$48,000 million), mainly on the basis of statistics of international public debt. Professor Hirsch (*Weltwirtschaftliches Archiv*, March 1933, page 327) estimates the total world international indebtedness at RM. 307,000 million (gold \$73,000 million). This figure includes, however, fixed property and shares owned abroad, and the debt of the Russian empire (RM. 17,000 million).

Total Foreign Gross Indebtedness of Certain Countries.
Gold \$(000,000's).¹

Country	Date	Total debt	Annual interest due	Total debt and direct investment	Annual interest, dividends, profits, etc.
Germany	Sept. 1932	4,670	250	5,860	310
Canada	Jan. 1930	.	.	6,125	273
Australia	1930	.	.	3,650	185
Argentina	1931	.	.	.	118
China	1931	763	56 ²	3,300	155 ²
India	1931	.	.	.	84
Union of South Africa	1931	.	.	.	69
Japan	Dec. 1929	1,150	48	1,280	52
Dutch East Indies	1932	.	36	.	49 ³
Poland	1930	.	.	1,130	49
New Zealand	March 1932	.	.	750 ⁴	30
Roumania	1932	965	41	.	.
Hungary	Dec. 1931	752	35	.	39
Greece	1932	472	.	515	27*
Czechoslovakia	Dec. 1931	318	23	356	26
Norway	Dec. 1932	373	15	427	17

It is not possible to give a complete record of the distribution of international indebtedness in the world according to debtor countries, but the above table, which shows the total foreign debt of a number of debtor countries, may indicate where the most important debtors are to be found.

It has proved impossible in most cases to separate the total of direct investment from that of borrowed capital. Fairly adequate estimates exist, however, of public international indebtedness. The following estimates have been compiled by the German Institut für Konjunkturforschung :

* 1931.

¹ Where no other source is indicated, see League of Nations *Balances of Payments, 1930, and Balances of Payments, 1931-32*, Geneva, 1932 and 1933.

Australia : R. Wilson, *Capital Imports and Terms of Trade*, Melbourne, 1931.
China : Remer, *Foreign Investments in China*, Macmillan Company, New York.

Japan : Moulton, *Japan*, Brookings Institution, Washington, 1931.

Roumania : Report by the Stresa Conference (League of Nations document C.666.M.321.1932.VII).

² These figures represent estimated payments (not amounts due) in 1930.

³ Dutch East Indies : interest, dividend and profits paid in 1929 were \$132 million.

⁴ New Zealand : The figure does not include short-term debt. At least \$615 million represent long-term debt as distinct from direct investment.

*Public International Indebtedness, excluding Political Debts.
Gold \$(000,000's).¹*

Country	State marketable debt			Debt of other public authorities	Total public debt
	Long term	Short term	Total		
Australia	2,525.3	—	2,525.3	102.0	2,627.3
India	1,638.3	—	1,638.3	—	1,638.3
Germany	617.4	84.7	702.1	566.1	1,268.2
Canada	577.5	—	577.5	961.9	1,539.4
Brazil	675.4	—	675.4	571.8	1,247.2
South Africa	784.4	—	784.4	204.8	989.2
Japan	696.9	—	696.9	116.8	813.7
New Zealand	606.7	—	606.7	48.2	654.9
Argentina	452.7	—	452.7	278.2	730.9
Mexico	203.8	284.1	487.9	4.4	492.3
Dutch East Indies	—	—	—	478.7	478.7
Poland	181.7	—	181.7	22.8	204.5
Roumania	396.3	—	396.3	—	396.3
Belgium	314.0	27.7	341.7	10.0	351.7
Hungary	215.1	21.1	236.2	137.4	373.6
Greece	322.4	9.7	332.1	—	332.1
Yugoslavia	311.2	—	311.2	7.0	318.2
Chile	301.5	—	301.5	26.7	328.2
Austria	199.9	11.9	211.8	45.9	257.7

It is clear that the total amount of external public debt must be considered in relation, not only to population, natural resources, economic efficiency and the type of expenditure for which loans were sought, but also in relation to the part played by the public authorities in economic life and to the possibilities of domestic borrowing. The statistics given should not be construed, therefore, as evidence of over-borrowing. The pressure upon the countries which produce large quantities of raw materials and foodstuffs for export has been very great, not only because the prices of those commodities fell much more than the average, but also because the agricultural countries are prominent among those which have the largest external debt payments to meet. The greater part of their obligations, it should be noted, consists of long-term debt which is not easily reduced or converted.

Calculations of the distribution of debt claims among creditor countries are rendered difficult by the fact that the holdings of marketable securities are readily shifted from one financial centre

¹ *Wochenbericht des Instituts für Konjunkturforschung, March 22nd, 1933.*

to another.¹ In addition to the rapid transfers of short-term credits which have been so marked a feature of recent years, financial insecurity has caused a great deal of speculative buying of securities.

The calculations of total international indebtedness given on page 262 exclude direct industrial investment. Studies of this problem demand prolonged investigation in each particular case.² There has been much buying of international industrial securities also in recent years.

It is practically impossible in such circumstances to bring up to date reasonably accurate estimates of the amounts of capital invested abroad by nationals of the main creditor countries. It has been estimated that British loans to dominion and foreign Governments, loan capital in British companies operating abroad and in foreign and colonial enterprises amounted at the end of 1932 to £2,222 million.³ An official calculation of United States portfolio investments abroad at the end of 1930 amounted to \$7,834 million, of which \$6,124 million were Government, municipal and Government-guaranteed loans, and the remainder (\$1,700 million) private corporate issues.⁴ If deductions are made for subsequent international security movements, and for shares included in the last-mentioned figure, the long-term bonded debt to the United States at the end of 1932 may be estimated at something in the neighbourhood of \$6,500 million.⁵

The estimates given above may also be utilised to indicate roughly the proportion which various debts represent of the total. Non-political public debt of central and local Governments has been estimated by the Institut für Konjunkturforschung as amounting to \$19,000 million, or a little less than the estimated long- and short-term commercial debt, which amounted to about \$21,000 million. Only a comparatively small proportion (probably

¹ Cf. Bank for International Settlements, "Third Annual Report", Basle, May 8th, 1933, page 12.

² Cf., e.g., C. F. Remer, "Foreign Investments in China", New York, Macmillan Company, 1933.

³ Sir Robert Kindersley, "British Foreign Investments", *Economic Journal*, March 1933.

⁴ *Trade Information Bulletins* 767 and 803.

⁵ Information for other creditor countries is scanty. There are estimates of the balance of payments in France which throw light upon interest receipts and capital movements, but no recent estimates of total investments abroad. The National Bank of Switzerland estimated the total of that country's long-term investments abroad at the end of 1930 at 6,500 million Swiss francs (*Bulletin Mensuel de la Banque Nationale*, March 14th, 1931). The League of Nations *Balances of Payments* indicates the source of information for other countries.

The Institut für Konjunkturforschung has estimated that the external public debts, including the debts of local authorities, but excluding political debts, was distributed according to creditor countries as follows, in gold \$(000,000,000's omitted):

United Kingdom	United States	France	Netherlands	Switzerland	Total
10.3	5.2	0.9	0.6	0.2	19.3

less than 5 per cent) of the public debt is on short term ; but a much larger proportion of commercial debt is for short periods. The Bank for International Settlements has estimated the total international short-term indebtedness in the world at the end of 1932 as 30,000 million Swiss francs (about \$6,000 million), of which approximately half "represented liabilities which were, in fact, governed by standstill agreements, moratoria, exchange restrictions, etc."¹ If allowance is made for governmental short-term debts, it appears probable that short-term loans account for about 25 per cent of the outstanding commercial debt. These short-term debts represent partly commercial borrowings ; but consist largely of moneys held by commercial banks on short-term deposit.

The country for which debt statistics are most adequate is Germany, where successive investigations have yielded a great mass of data.² The general movement of non-political international debt in that country may be summarised in the following table :

*Non-political International Indebtedness in Germany.*³
RM.(000,000,000's).

	July 31st, 1931	November 30th, 1931	February 29th, 1932	September 30th, 1932
Short-term debt (including debt subject to standstill agreements) . .	13.1 (6.3)	10.6 (5.4)	10.1 (5.0)	9.3 (4.3)
Long-term debt	10.7	10.7	10.5	10.2
Total	23.8	21.3	20.6	19.5

Of the total indebtedness at the end of September 1932, different types of creditors in foreign countries held the following amounts of long- and short-term debt :

	RM.(000,000,000's).	
	Long-term	Short-term
Banks	1,234	6,442
Financial companies	669	524
Traders and industrialists .	203	1,563
Other creditors	8,075	818
Total	10,181	9,347

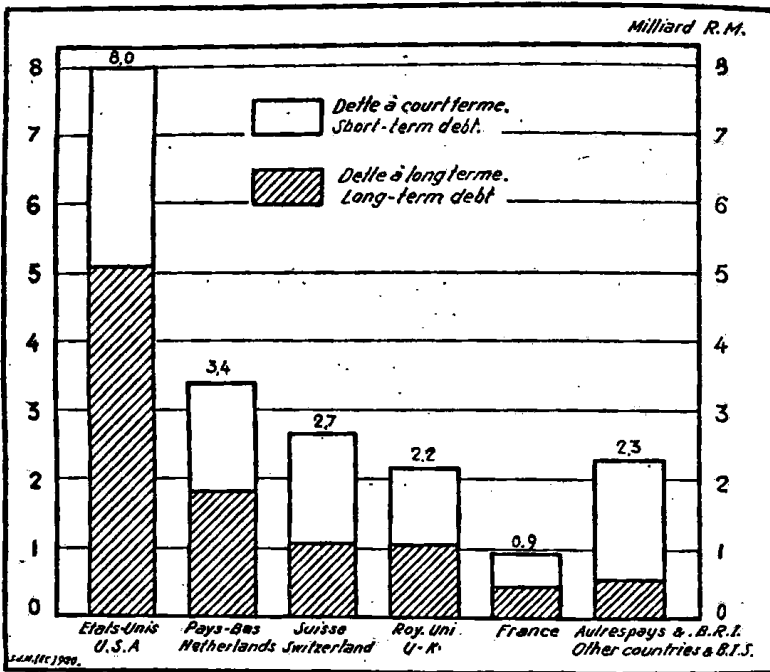
¹ Bank for International Settlements, "Third Annual Report", Basle, May 8th, 1933, pages 11 and 12.

² *Wirtschaft und Statistik*, 1. Mai Heft, 1933.

³ The figures include only those groups of debt which were included in the census of September 1932.

The distribution among creditor countries is shown by the following diagram and table :

*Distribution of German Non-political External Debt
at September 30th, 1932.*
RM.(000,000,000's).



Creditor country	Long-term	Short-term	Total
	RM.(000,000,000's).		
United States	5,118	2,898	8,016
Netherlands	1,868	1,559	3,427
Switzerland	1,096	1,611	2,707
United Kingdom.	1,060	1,171	2,231
France	465	399	864
Other countries and B.I.S.	574	1,709	2,283
Total	10,181	9,347	19,528

An incomplete summary table of short-term indebtedness in some other European countries may perhaps be added in order to show the general nature of the problem.

*Short-term Indebtedness of Certain European Countries.*¹
\$(000,000's).

Country	Date	Short-term indebtedness of					Total
		Central Government	Local authorities	Central Bank	Other banks	Other debtors	
Austria	IX. 1932	14.1	0.3	121.9		19.4	155.7
Hungary	XI. 1931	42.8	21.8	25.3	106.7	124.0	320.3
Bulgaria	XII. 1931	4.2	3.4	1.1	10.3	23.4	42.4
Poland	XII. 1931	0.4	—	5.1		27.9	33.4
Roumania	1932	.	.	13.5	23.7	41.9	79.1
Denmark	XII. 1932	.	—	25.0		36.2	61.2
Finland	XII. 1932	7.5	1.4	4.7	24.4	17.5	55.5
Norway	I. 1933	2.2			19.7	106.9	128.8
Germany	IX. 1932	148.0		193.6	918.4	963.3	2,223.3

THE PROGRESS OF DEBT ADJUSTMENT.

From the information given in the preceding section, it should be clear that the problems of international indebtedness are not only complex but vary a great deal from country to country. The freezing of short-term debt is most difficult in certain European and South American countries, and is greatly complicated by the measures of exchange control which have been found necessary to maintain currency stability. In most of those countries and in a number of others, the external payments on account of long-term debt have also been interfered with by the depression, and a series of temporary expedients

¹ Austria: League of Nations, "Financial Position of Austria, Third Quarter 1932" (C.780.M.368.1932.II.A).

Hungary: *Revue Hongroise de Statistique*, August 1932.

Bulgaria: *Bulletin Mensuel de la Banque Nationale*, February 15th, 1932.

Poland: *Informations Statistiques* 1932, page 273.

Roumania: Report by the Siresa Conference (League of Nations document C.666.M.321.1932.VII).

Denmark: *Statistiske Efterretninger*, May 1933.

Finland: *Nordiska Föreningsbanken, Uttilas*, February 1933.

Norway: *Statistiske Meddelelser*, Nr. 4-5, 1933.

Germany: *Wirtschaft und Statistik*, 1. Mai, Heft, 1933.

have been adopted to relieve the strain on the balance of payments.

The pressure of the external debt service upon the weaker debtor countries was heavy even before the acute phase of the financial crisis began in the early summer of 1931; but the currency instability provoked by that crisis, the violent movement of short-term funds from one centre to another, hurriedly improvised trade restrictions and foreign exchange controls rendered inevitable a series of emergency, debt suspensions and partial or total defaults. These emergency measures followed one another in rapid succession during the second half of 1931 and continued, and were even added to, in 1932 and the first months of 1933; but the relief obtained from the depreciation of sterling became clearer when the financial crisis eased off in the summer of 1932. At the same time, there set in a series of adjustments by which the debt burdens of many countries were further lightened.

It is a hopeless task to attempt any exhaustive review of the different measures adopted in the various countries, and neither possible nor useful to make a statistical computation of the total amount of debt affected by them. As the illustrative examples given later indicate, each country has its own set of problems which, indeed, need to be considered separately in the case of each transaction. The whole trend of policy has been against generalised solutions. Negotiations have taken place in certain cases between debtor Governments and representatives of creditors. The general problem has also been discussed at successive international conferences, notably at Stresa and London. These discussions are reviewed later in this section. Meantime, it is sufficient to point out that the principle upon which such discussions have proceeded is that stated in the draft annotated agenda of the Monetary and Economic Conference that "the settlement of this question is essentially the concern of the creditors and the debtors themselves".¹

It is convenient first to illustrate the difficulties that arose in the payment of short-term debt obligations. Short-term credits are normally extended primarily to finance trade and particularly international trade. Commodities are shifted from producer to merchant and from merchant to consumer — often in widely separated countries — by means of credit advanced from leading financial centres. Thus the farmer who delivers cattle to a refrigerating concern in the Argentine, the exporter of manufactured goods from Germany or Austria, the dairy-farmer who delivers cream to a co-operative factory in New

¹ Draft Annotated Agenda, page 22.

Zealand, are enabled to draw cash payments for their produce. These payments are made possible either by advances against future sales of the finished product or by discounting bills of exchange which will not be met until their maturity after delivery of the goods. The credit needed for these purposes is advanced by bankers in the great financial centres until the consumers complete the chain of transactions by paying for their purchases. There is normally, therefore, a considerable amount of international short-term commercial debt constantly being liquidated and renewed. In addition to such commercial debt, there is a small amount of governmental short-term borrowing in foreign money markets.

During the boom period and the earlier years of the depression there was, on the other hand, a considerable accumulation of short-term foreign balances by those countries which either had gold-exchange standard currencies or made considerable use of foreign exchange holdings in their Central Bank reserves. The liquidation of these foreign balances after the financial panic, which was described in Chapter VIII, considerably reduced the amount of short-term indebtedness in the world; but this liquidation was accomplished mainly by the creditor countries which remained on the gold standard.¹ It did not relieve the position of the debtor countries which had large short-term indebtedness and small short-term foreign assets to set against them.

In a few debtor countries, short-term advances had been made by the more powerful Central Banks and the Bank for International Settlements to enable the Central Banks to withstand currency drains in the early part of the depression. These advances were not a source of difficulty, since they were readily renewed; but considerable difficulty arose from the fact that the commercial banks in some of these countries were caught with heavy short-term obligations and illiquid long-term assets.

When the financial panic in the early summer of 1931 was followed by a widespread abandonment of the gold standard, protective trade restrictions were redoubled and international trade decreased further both in quantum and in value. Amounts of short-term credit that had been adequate to finance trade at its former value became redundant, but in many cases impossible to repatriate. At the same time, a considerable amount of short-term credit unable to find investment accumulated and was apt to be transferred rapidly from one financial centre to another. The transfer problem first became acute in connection with these short-term debts, and its first manifestations were

¹ Cf. also Bank for International Settlements "Third Annual Report, April 1st, 1932, to March 31st, 1933", Basle, May 8th, 1933, page 10.

naturally in those countries which, besides having excessive commercial obligations, were burdened also with short-term advances to commercial banks. In the summer and autumn of 1932, therefore, it became necessary to devise temporary arrangements for the suspension of transfers primarily on account of commercial and banking short-term debt. Defaults, partial or complete, transfer moratoria, suspensions of sinking funds and interest payments on long- as well as short-term debt, together with all the accompanying phenomena of blocked accounts, developed later as the depression became still worse towards the end of the year.

It is convenient for purposes of illustration to deal first with the arrangements made to cope with the situation in Germany, which, though not the first in point of time, was of the greatest magnitude and presented in many respects the greatest dangers to international economic equilibrium.

The London Conference (July 20th to 23rd, 1931) was followed by the appointment by the Bank for International Settlements of an expert Committee to enquire into the financial position of Germany. That Committee met at Basle on August 8th, 1931, and concurrently a Committee of creditors — including representatives of American, British, Swiss, Dutch, French, Swedish, Italian, Belgian, Danish, Norwegian and Czechoslovak banks — arranged the first German standstill agreement, by which payments were suspended on account of short-term debt amounting to about RM. 6,300 million (including the "theoretical" sums covered by the agreement but not actually registered to the amount of roughly RM. 300 million). The agreement, which came into force on September 17th, 1931, was for a period of six months dating from September 1st. The mass of debt covered by this agreement consisted of a great number of obligations of different sorts and subject to different conditions, payments on all of which were suspended. A large amount of short-term indebtedness, however, was not subject to this agreement and much of this was liquidated in the usual way.¹

Before the expiry of this agreement, a new arrangement was made in February 1932 extending the standstill arrangements till the end of February 1933. Ten per cent of the outstanding amounts was, however, paid at that time. In February 1933, the agreement was renewed for a further twelve months till the end of February 1934, a further 5 per cent being repaid. By this time, however, the amount outstanding was reduced

¹ The standstill agreement related to banking investments in Germany, the total amount of which was RM. 7,600 million. The total short-term foreign debt in July 1931 was estimated at RM. 13,100 million.

to about RM. 3,800 million (plus the RM. 300 million "theoretical" amounts), partly by the percentage repayments mentioned above, partly by other forms of repayment. By various means, including offsetting transactions not requiring the transfer of foreign exchange, debtors had found ways of meeting a considerable part of their obligations. Tourist and similar expenditures in Germany had been met by drawing upon balances in German banks, capital assets were purchased and other forms of converting the short-term debt were utilised, while in certain cases "supplementary exports" beyond those for which foreign exchange received in payment had to be surrendered were used as payments for the debts.¹

The original standstill agreements were complicated by many provisions concerned with related problems, such as disposition of balances held in German marks, security on the loans, interest rates and payments. They were supplemented also by another standstill agreement concluded on April 9th, 1932, covering RM. 247 million of short-term debts owed by eight German Federal States and twenty-six municipalities and districts. Ten per cent of the amount due, less repayments made after July 1931, was paid on the signature of the agreement. Interest rates were reduced from an average of 9 per cent to a basic rate of 6 and a possible maximum of 8 per cent. This agreement was renewed in March 1933, on a further repayment of 5 per cent, half in March and half in October, while the basic rate of interest was reduced from 6 to 5 per cent.

There were interest reductions also under the main standstill agreement, in April and July 1932; but, when the agreement for the second time was renewed for twelve months in March 1933, the creditors contested further interest reductions, which however, were lowered again to $4\frac{3}{4}$ per cent for cash credits, and to $3\frac{1}{8}$ - $4\frac{1}{2}$ per cent for acceptances given to banks, and to $5\frac{3}{4}$ per cent for cash credits and 5 per cent for acceptances given to industrial and commercial firms. While, as was stated above, the repayment of capital on this renewal was only 5 per cent, the reductions of interest rates and of indirect methods of payment steadily lowered both the burden of debt service and the outstanding capital amount.

The Austrian standstill agreement on June 16th, 1931, was the first of the series. Foreign creditors of the Credit-Anstalt agreed to a suspension of payments for two years on condition that the Austrian Government guaranteed the debts amounting

¹ Cf. Bank for International Settlements "Third Annual Report, April 1st, 1932, to March 31st, 1933", Basle, May 8th, 1933, page 12.

to 500 million schillings (\$71 million). A second standstill agreement between other Austrian banks and their foreign creditors, including a system of amortisation, covered debts amounting to 240 million schillings. When this second agreement was renewed on January 20th, 1932, the amount outstanding had fallen from 240 to 114 million schillings, and a further 6 millions was repaid in the first half of 1932. The agreement was further renewed early in 1933 till January 15th, 1934.

An agreement with the foreign creditors of the Credit-Anstalt had been initialled on January 21st, 1933, but it was found necessary to negotiate a modification of this agreement, and, on May 12th, the final arrangements were formally ratified by the Austrian Government. Liabilities of the Credit-Anstalt amounting to 400 million schillings were to fall due on June 1st; but the funding of these liabilities, together with the improved state of the Austrian public finances, the re-organisation of the banking system, the renewal of the second standstill agreement till January 15th, 1934, and the prospect of a further loan, relieved the pressure on the Austrian balance of payments. The discount rate of the National Bank was reduced on March 24th from 6 to 5 per cent. Private clearing agreements were gradually extended until the National Bank was able, on April 6th, virtually to relinquish control of foreign exchange. In the course of this operation, the depreciation of the currency was recognised in practice, whereupon the rate ruling in commercial transactions improved substantially.¹

The Hungarian standstill arrangements proved more difficult to negotiate; but, on November 8th, 1932, almost a year after a moratorium had been imposed on transfers, an agreement was concluded with British and American investors. Individual arrangements were made also with creditors in certain other countries. On February 1st, 1933, a new standstill agreement for one year was agreed to by American, British and Swiss creditors. By this time, the methods of administering standstill agreements had been standardised, and the Hungarian agreement contained the usual provisions concerning interest, repayment in pengö at the creditors' option, together with the possibility in certain circumstances of utilising these blocked pengö accounts for payments within Hungary, for example, by tourists, 5 per cent reduction of the capital and further voluntary repayment subject to the assent of the National Bank.

¹ More detailed information concerning the financial position in Austria, Hungary, Roumania, Bulgaria and Greece may be found in the regular reports of the Financial Committee to the Council of the League of Nations and in the quarterly reports of the League representatives in Austria, Hungary and Bulgaria.

The history of these standstill arrangements shows how a difficult debt situation has gradually, by goodwill on both sides, approached a manageable solution. Though the negotiations proved arduous and complicated, the good faith of the debtors combined with reasonable concessions on the part of the creditors has already brought about a substantial diminution of short-term indebtedness and an even greater reduction of the annual interest burdens. The standstill agreements, it should be made clear, are in respect mainly of banking credits and cover indebtedness contracted mainly in Germany and to a less extent in Austria and Hungary, the countries where short-term borrowing by banks was most pronounced in the early stages of the depression.

The transfer difficulties in respect of short-term debt are well illustrated also by the situation that arose in the Argentine. For thirty years, from 1899 to 1929, the external value of the peso was stabilised by the operations of the Conversion Office, which, in effect, administered a gold-exchange standard system based on London. The operations of the Conversion Office were suspended on December 29th, 1929, in consequence of a considerable flight of capital. The internal and external value of the peso depreciated until, in October 1931, the latter was 82 per cent below the parity formerly maintained. On October 10th, 1931, the Government instituted a system of exchange control which had the effect of stabilising the currency, but in doing so froze a certain amount of short-term debt for which transfer resources could not be arranged. Available foreign exchange was allocated to importers, to national, provincial and municipal financial services, to residents abroad, and to public utility and private companies. The latter suffered most heavily, and some of them were unable to meet their obligations abroad although they had earned the necessary profits in Argentine currency. On May 1st, 1933, however, an agreement was entered into with Great Britain whereby a loan was made available to provide the means of liquidating transfer arrears, and at the same time mutually satisfactory arrangements were made for future transfers. In effect, the short-term debt which it had been impossible to transfer was liquidated by a long-term loan issued to the Government.¹

Short-term debt, however, is the smaller part of the general problem, and the general deterioration of the economic situation during the depression, and especially during 1932 and the early

¹ Cf. Dr. Guillermo E. Leguizamon, K.B.E., "An Argentine View of the Problem of Exchange Restrictions", *International Affairs*, July-August 1933, pages 504-517.

part of 1933, rendered inevitable a succession of suspensions of debt service, either in part or as a whole, on both short- and long-term debt of private and public character in many countries. In certain cases, such suspensions applied only to the transference of the debt service, interest and amortisation payments being "blocked" in special accounts held in national currencies. In other cases, there was default, either partial or complete. In the discussion which follows, an effort is made to distinguish these phenomena.

The transfer problem is obviously influenced by the widespread imposition of exchange controls designed to protect national balances of payments and ultimately to safeguard the stability of national currencies. As international trade shrank, the demands of foreign debt service upon the diminishing amounts of foreign exchange available became proportionately greater. The point was soon reached in one country after another where it was impossible to provide the exchange necessary for debt payments. It was, however, eased in many cases, as far as sterling debt was concerned when the United Kingdom abandoned the gold standard and still further eased when the dollar depreciated.

There have been three principal phases of development in the situation. The first, which covers roughly the first years of the crisis to the end of 1931, consists mainly of a series of defaults on the part of weak debtor States, mainly in South America. As successive reports of such bodies as the British Council of Foreign Bondholders indicate,¹ there is a substantial amount of indebtedness in the world, default on which has been a problem for many years. No adequate study exists either of the proportion of foreign lending which has fallen into default in recent years, or of the methods which have been adopted to deal with such defaults. Since 1929, the arrears of default, both of interest and sinking funds, have accumulated and new defaults have occurred. In the period under consideration, Ecuador, Mexico and Turkey, for example, have not been able to resume payments, while new defaults by central or local authorities occurred during 1931 in Bolivia, Peru, Chile, Brazil, Uruguay, Argentine, Dominica and Colombia. This development continued in the early months of 1932, Nicaragua, Salvador, and China being added.

A new phase was ushered in, presaging the financial panic which broke in the spring of 1932, when in December 1931, Hungary was forced unilaterally to declare a transfer moratorium upon external debt service with the exception of that on the League loan. In this case, the payments were continued in

¹ Cf., e.g., "Fifty-ninth Annual Report of the Council of the Corporation of Foreign Bondholders for the Year 1932", London, Council House, No. 17, Moorgate.

Hungarian currency, but could not be transferred to creditors for lack of sufficient foreign exchange. Bulgaria, in April 1932, made an arrangement with the holders of Government loans to reduce the amount of debt service transferred to 50 per cent of the amount due. That percentage was further reduced to 40 per cent after November 1932 and to 25 per cent after April 15th, 1933. In April, Greece, after similar negotiations, suspended the transfer of payments on account of sinking funds and in May reduced the interest payments on public debts transferred to 30 per cent. By agreement with the foreign bondholders in September 1932, interest payments were to be reduced to 30 per cent ; but further controversy arose, and, despite repeated negotiations, no settlement had been reached at the time of writing (July 1933).¹

In June 1932, Austria suspended the transfer of debt service on all foreign debt, public and private. There was a partial resumption transfer from the beginning of 1933, but on account of the delay in floating the loan provided for in the Geneva Protocol of July 15th, 1932, transfers were again suspended early in the year.² In November, Yugoslavia also failed to transfer her debt service and, in January 1933, negotiated a three-year moratorium with her creditors. In January 1933, also Roumania, after consultation with foreign bondholders' associations, suspended, with certain exceptions, amortisation payments. For one and possibly two years, therefore, Roumania agreed to transfer full interest but only a small part of the repayments due on Government loans. At the same time, however, the right was reserved to re-open negotiations with the bondholders if the budgetary receipts for the first five months of the financial year 1933-34 proved unsatisfactory or if the balance of payments did not yield the necessary foreign exchange. Notice was given in July that this right would be exercised. Meantime, defaults had occurred in Costa Rica (December 1932) and Cuba (March), while Paraguay followed in June.

The third phase opened in June, shortly before the Monetary and Economic Conference was convened, by the announcement that Germany was forced to contemplate a transfer moratorium on all her foreign debt except that covered by the standstill agreements. Negotiations began almost immediately in London, and agreement was reached by which interest rates were reduced and repayments deferred upon the debt covered by the standstill agreements. The long-term debt situation was discussed also, and it was agreed that interest should have priority over

¹ Cf. League of Nations Financial Committee "Report to the Council on Greece", July 8th, 1933 (II. Economic and Financial : 1933.II.A.14).

² Cf. League of Nations "Quarterly Reports on the Financial Position of Austria".

amortisation payments, the service of the Dawes loan having absolute priority. The President of the Reichsbank also agreed to give consideration to the request of the creditors that the Young loan payments should follow in priority. A suggestion that the sinking fund payments on the Young loan should be temporarily postponed in order to accelerate the recovery of the exchange position was referred to the Bank for International Settlements.¹

The position when the Monetary and Economic Conference discussed the problem of international indebtedness in early July, therefore, had entered upon a new phase. Recent defaults, additional to continuing default on the part of several countries, had occurred in Bolivia, Peru, Chile, Brazil, Uruguay, Argentine, Dominica, Colombia, Nicaragua, Salvador, China, Costa Rica, Cuba and Paraguay. Transfer moratoria, accompanied by such measures as reductions of interest payments or suspensions of sinking funds, had been declared in Bulgaria, Greece, Yugoslavia and Roumania. Other transfer moratoria which did not envisage reductions of debt service were in force in Hungary and Austria, while another was under discussion for Germany and came into force on July 1st. In addition to the blocked accounts created in several of the countries which had ceased to transfer debt service but continued payments in domestic currencies, the foreign exchange controls of many other countries had resulted in foreigners' balances being blocked. Altogether, there were such blocked accounts, or accounts virtually blocked, in twenty-two countries — in Austria, Bulgaria, Germany, Hungary, Greece, Roumania, Yugoslavia, Angola, Argentine, Brazil, Chile, Costa Rica, Colombia, Nicaragua, Turkey and also in Czechoslovakia, Denmark, Estonia, Iceland, Latvia, Persia and Venezuela.

The usage of these blocked accounts varies a good deal.² In most countries, they are available for internal payments, and can be drawn on for tourist and similar expenditures, sometimes freely, but in other cases only with the permission of the Central Bank. There has been a certain amount of funding of these balances either by the issue of long-dated Government scrip or long-dated bills or by the purchase of industrial securities. In June 1933, for example, an agreement was reached between the Bank of Brazil, the Brazilian Government and representatives of certain creditors by which the creditors delivered to the Bank their balances in Brazilian currency, the Bank converting them into dollars and delivering to the creditors seventy-two equal bills of exchange payable monthly. In Colombia, Government

¹ *London Times*, June 17th, 1933.

² Cf. *Royal Institute of International Affairs, "Monetary Policy and the Depression"*, London, Oxford University Press, 1933, pages 93-118.

scrip with a ten-year currency was offered in payment of debt service after December 1931. In European debtor countries, such funding as has been effected has been by private arrangement between debtors and creditors. The Yugoslav Government, however, has concluded a funding arrangement.

The position of the debtor countries may be summed up, therefore, by pointing out that circumstances have forced some adjustments of their burdens, but that the major problems as yet remain unsolved. There have been substantial reductions of short-term debt, and various moratoria and suspensions of transfer, with some default on longer-term obligations. In addition, it should be emphasised that the real burden of external indebtedness has been greatly relieved by the exchange depreciation of the sterling and dollar currencies in which so large a proportion of the world's foreign debt is reckoned. A depreciation of 25 to 30 per cent in these currencies has been equivalent to a similar reduction of the nominal cost of debt service where the national currencies of debtor States have not further depreciated. Certain countries of the gold *bloc*, however — France, Belgium and the Netherlands — have paid debts falling due in gold dollars, ignoring the abrogation of the gold clause by the United States. The United Kingdom in July paid a dollar debt in paper dollars, but at the same time offered a conversion arrangement which, in effect, gave a premium to the creditors more than the current value of the dollar but less than gold parity.

Moreover, the tendency since March 1933 for the general level of wholesale prices to rise is a definite gain, though the extent of that gain is limited by the extent to which the exports of debtor countries remain subject to unusual import restrictions. A rising price level, accompanied by freer trade, would go far to solve the major problems of indebtedness.

There remain, however, very difficult cases of individual countries and of individual loan transactions in those countries which are not likely to be met by any measure of currency devaluation, freer trade, or rising prices that seem to be in prospect. For cases of over-indebtedness or unwise borrowing, more radical solutions will no doubt eventually be found. Discussion of this problem has been somewhat confused by the natural concentration of debtors upon their present situation, against which must be set an equally natural reluctance of their creditors to conclude permanent arrangements at the depth of the depression. The Stresa Conference in September 1932,¹ the meetings

¹ League of Nations, Commission of Enquiry for European Union, "Report by the Stresa Conference for the Economic Restoration of Central and Eastern Europe" (document C.666.M.321.1932.VII).

of the Preparatory Commission of Experts who drew up the draft annotated agenda of the Monetary and Economic Conference in January 1933,¹ and the Conference itself in June and July 1933, devoted a good deal of consideration to this general problem. The resolution finally passed by the Monetary and Economic Conference at its plenary session on July 27th laid down a series of general principles — the necessity of freeing trade, the sanctity of contracts, and the desirability of creating organisations of creditors with which debtors might negotiate.²

The last principle has, in fact, emerged from the difficulties of recent years. The British Council of Foreign Bondholders — the prototype of such organisations — as founded in 1868, licensed by the Board of Trade in 1873 and reconstituted in 1898 by special Act of Parliament. Its principal object is “the protection of the interests of the holders of foreign securities”; but, in pursuit of that interest, it acquires a great deal of valuable financial information and serves not only as an instrument of negotiation with debtors, but also as a source of information regarding the possibilities of future investment. A similar organisation exists in France, and another has recently been created in the United States. *Ad hoc* committees of creditors have been formed in other countries in recent years including the League Loans Committee formed to protect the interests of bondholders whose loans were guaranteed by the League of Nations; but, in endeavouring to negotiate standstill and other agreements, debtor Governments have been handicapped by the incomplete organisation of creditor interests as a whole. It is to remedy this difficulty that the Conference resolution on indebtedness included the suggestion that such organisation should be improved, and that co-operation should be fostered between the various national bodies representing creditor interests. Cautious steps in this direction are obviously of great importance in view of the large rôle played by international lending in the economic life of the modern world.

¹ League of Nations, Monetary and Economic Conference, “Draft Annotated Agenda submitted by the Preparatory Commission of Experts” (document C.48. M.18.1933.II).

² League of Nations: *Journal of the Monetary and Economic Conference*, London, 1933.

Chapter X.

THE BALANCING OF INTERNATIONAL ACCOUNTS.

THE PROBLEM OF INTERNATIONAL EQUILIBRIUM.

The subjects treated in the preceding chapters of this *Survey*, and particularly in those devoted to international trade, monetary and banking policy, and international indebtedness, may all be regarded as different aspects of one great problem — that of restoring balanced equilibrium in the economic system. The conception of equilibrium, it is true, presents considerable difficulties in economic discussion, mainly because such equilibrium as exists in practice is the unstable, shifting result of an almost infinite series of temporary and incessantly changing minor equilibria. Much of the interest and value of economic analysis lies, not only in the study of theoretically stable positions of equilibrium, but also in that of the departures from equilibrium which are the occasions of economic change and development. Thus the study of international trade and of the forces which tend to regularise and balance imports and exports leads naturally to analysis of the processes by which population and capital resources have been transferred from more to less developed regions and have thus greatly facilitated the building up of important new units of economic organisation. The international commerce which developed so rapidly in the nineteenth and twentieth centuries is remarkable, not only because of the regularity and efficiency with which adjustments were made and new equilibria achieved in the national economic organisations of the countries which participated in that commerce, but also because it was the vehicle by which a "new world was called into existence to redress the balance of the old".

In the *Survey* for 1931-32 an attempt was made to explain the dynamic nature of the processes by which international accounts are balanced, not as the result of a calculation at stated periods, but continuously by the interaction of a whole series of

economic and financial forces — rates of interest and levels of prices as well as amounts of credit and quantities of goods and services interchanged.¹ Stress was there laid upon the inherent tendency of these forces to restore equilibrium between the national economic systems. But the same conception may also be used as a starting-point from which to analyse the phenomena of development as distinct from those of equilibrium. It is, in fact, not a static position of equilibrium which is achieved through the interaction of these international financial and economic relationships, but a continuous series of adjustments to a shifting equilibrium. As much importance attaches to the shifting trend as to the adjustments which keep a balance between the national economic systems as the trend develops.

It is necessary, if this dynamic conception is to be fruitfully used, to recognise clearly that current economic analysis and popular discussion which begin by assuming closed national economies, even if at a later stage some modifying “international” factors are introduced, run the risk of disregarding important elements of the problem. There is, at the present time, little risk of the contrary assumption of a world economic unit being made. Most economic discussion is concentrated upon the effects of different phenomena upon the national dividend, and tends to minimise, or even ignore, the importance of parallel developments in respect of the national dividend of other countries.

It is essential, however, to realise that the real form which modern economic organisation has taken is neither that of a series of isolated national units nor that of a single economic world unit, but that of a series of partly closed, partly interdependent national economies linked in a shifting equilibrium, the changes in which are expressed by alterations in the rates at which the respective national currencies are exchanged. As was pointed out in the preceding *Survey*,² it was the strain which developed when the factors of interdependence (mainly financial) between national economies moved in such a way as to demand excessive adjustments of important domestic factors that threw the economic organisation of the whole world into confused disequilibrium.

The realistic consideration of economic problems is possible, therefore, only in this setting of international interdependence, as distinct from either national economic independence or cosmopolitan dreams of world unity. Nor is it possible to separate national from international equilibrium. There can be no stability of national economic organisation which does not presuppose either

¹ *World Economic Survey*, 1931-32, pages 167-171.

² Pages 43-46.

complete isolation or else a relatively stable equilibrium with other national units—and isolation is, in fact, impossible in the modern world. The various factors that enter into national economic organisation exert their influence through the prices of commodities and services of all kinds; but each national price system is influenced by every other, if only because international competition constantly tends to render equal the local prices of important basic commodities.

These considerations derive added importance at the present time from the fact that the mechanism of the foreign exchanges by which normally the national price systems are connected has been impaired over a wide area. As long as it was possible to maintain the international gold standard, adjustments were automatic. When, for any reason, prices in one country got unduly out of relation with those in other countries, movements in the exchanges set up corrective forces which might be termed gyroscopic in character. If the price-levels were too high, goods flowed in and, if necessary, gold flowed out, till the levels had been brought back again to stable relationship with those of other countries. The extraordinary smoothness and efficiency with which these automatic adjustments were effected disguised the complexity of the processes involved. When exchange rates moved against a country in such a way as to render necessary a restriction of credit in order to safeguard the stability of the currency—in other words, to ensure a maintenance of international economic equilibrium—that restriction led to very intricate and complicated consequences. Not only was the average level of prices depressed, with all the consequences of disturbed equilibria between production and purchasing power, wages and costs of living, wholesale and retail prices, interest rates and other costs of production, but the prices of individual commodities and services and the conditions of their production and distribution were altered also. It is true that the range of alteration necessary was not, as a rule, great. It was only when there existed a fundamental cause of disequilibrium, such as the growing inflexibility of certain prices, that the cumulative effect over a long period of day-to-day adjustments in one direction caused serious difficulties in maintaining international equilibrium.

Since the breakdown of the gold standard, the multiplicity of the factors at work has not only become more obvious, but the disequilibria to be corrected are greater and the flexibility of prices which alone makes continuous adjustment possible has given way to more violent fluctuations of certain prices accompanied by more rigid flexibility in other parts of the price structure. The attempts which must inevitably be made to achieve international equi-

brum between the national economic systems are rendered vastly more difficult. Instead of the factors which must be adjusted being gathered up smoothly and automatically by the working of the gold standard, they must be considered separately. Moreover, the normal controls which keep them together having been broken, they have tended to fly apart and to fluctuate independently and more widely.

Perhaps the best illustration of this problem is to be found in the difficulty which surrounds discussion of the exchange rates which are actually in operation, of their relation to what might be a true equilibrium rate, and of the most suitable rates that might in the future be adopted as the basis of a new and lasting equilibrium between the national price systems. If answers are desired to the questions whether, at a particular rate, a currency is under- or over-valued, or whether permanent stabilisation might be possible at certain rates, very complex considerations must be taken into account. The diversity of opinion entertained in regard to these questions is a natural reflection, not only of the legitimate differences of opinion that may be held, and of the relative weight to be attached to various factors in the equation, but also of the virtual impossibility of measuring, and still less of forecasting, the development of many of the more important of them.

Thus, it is not sufficient merely to consider the relative levels of wholesale prices in the countries concerned. Setting aside for the moment the very important movements of short-term credit that are induced at short notice either by speculative possibilities or by flights from currency instability, there are very complex difficulties created by the divergent movements and variant flexibility of different sorts of prices within each country. Moreover, monetary policies pursued in the present circumstances of managed currencies are an extremely important element in the problem. At any moment it is difficult to find ratios — which must necessarily be multilateral — that exactly fit the needs of not only wholesale but retail price-levels, the cost of living, wages, export and import prices, the balance of trade, etc., in all the countries concerned. That difficulty is all the greater because the factors change incessantly from day to day, especially when the monetary policies of important countries are still in process of development.

No doubt, as monetary policies become more defined, and their results become more evident, the range of exchange fluctuations will gradually narrow and experimental *de facto* stabilisation within fairly wide limits be effective. The possibilities of holding fluctuations within such limits depend, obviously enough, not only upon freedom from new and violent disturbances, but also

upon the achievement of sufficient flexibility within national price systems to bring into line such domestic factors as are out of harmony with the equilibrium gradually developed.

THE BALANCE OF COMMODITY TRADE.

Detailed statistics of foreign trade in 1932 are not yet available for all countries, but an enquiry into the geographical distribution of the trade of fifteen important countries, the aggregate trade of which represents about 60 per cent of world trade,¹ reveals the fact that bilateral trade (the value of imports offset by exports to the same country) fell, in 1932, to 37 per cent of its value in 1929. Triangular trade (the value of imports offset by exports to other countries than that from which the imports are derived) fell to 30 per cent of its 1929 value. The aggregate net balances of commodity trade (imports or exports not offset but paid for by invisible items of export or import) fell only to 61.4 per cent of the 1929 figures.

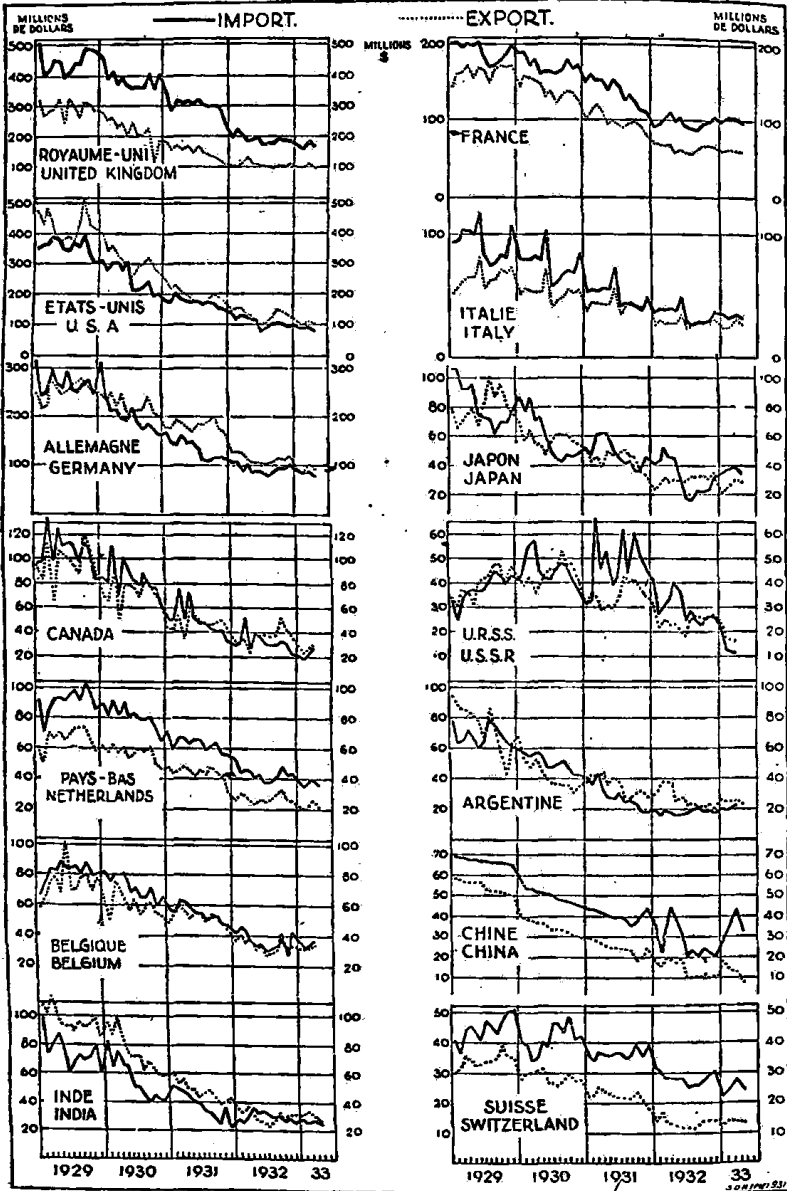
The following table shows the value, movement and distribution of the three groups :

	Gold \$ (000,000's)			Percentage movement			Percentage distribution		
	1929	1931	1932	1929	1931	1932	1929	1931	1932
Bilateral trade	26,999	15,269	10,011	100	56.5	37.1	72.0	66.9	69.3
Triangular trade	6,423	3,313	1,926	100	51.6	30.0	17.1	14.5	13.3
Aggregate net commodity balances	4,106	4,238	2,520	100	103.2	61.4	10.9	18.6	17.4
Total	37,528	22,820	14,457	100	60.8	38.5	100	100	100

The aggregate net commodity balances, which represent mainly the net outward or inward payments on account of fixed debt charges and of services, reveal significant movements in these years. In the period from 1929 to 1931, these balances increased, in spite of the great decline in trade, but from 1931 to 1932 they fell more than any of the other groups. This appears to indicate that, in 1932, the full payment of debt service proved impossible in face of the decline of world trade. The tendency in 1932 for the difference between import and export values to diminish is demonstrated by the diagram given below.

¹ League of Nations *Review of World Trade, 1932*, Geneva, 1933, page 62.

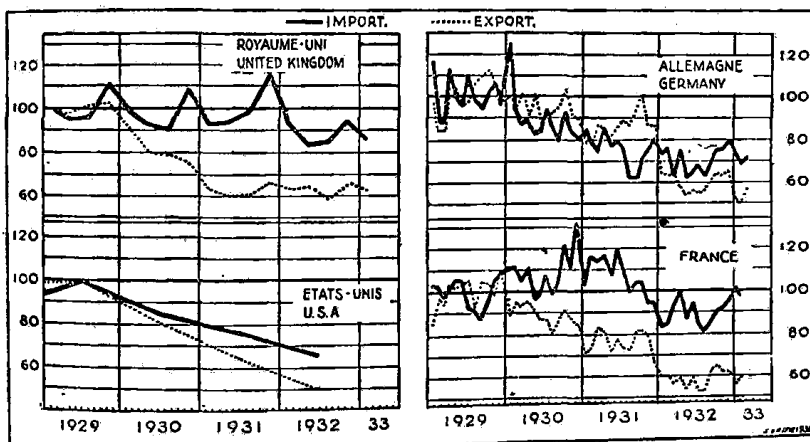
Imports and Exports of Certain Countries.
 Values in gold \$ (000,000's).



Inspection of the commodity imports and exports for a number of countries during the four years 1929-1932 below reveals a number of forces at work. Up till the end of 1931, the tendency was for creditor countries to find their passive balances increasing and for debtor countries to increase their active balance. Thus the passive balance (in million dollars gold) in France rose from 333 in 1929 to 464 in 1931, declining to 398 in 1932. Among debtors, Germany converted a passive balance of 173 in 1929 to an active balance of 384 in 1931, but was unable to maintain this figure, the active balance in 1932 shrinking to 242. There were many cases, however, where it was impossible for the debtor countries to make headway against the fall in prices. China, Spain, Hungary, the Irish Free State, British Malaya, and the U.S.S.R. are cases where, after an initial improvement, the balance of trade became more adverse. The statistics of India need special explanation, the smaller active balance of commodity trade being the counterpart of large exports of gold released from hoarding.

The trade values recorded are the result of two factors — the quantum of trade and relative prices. It will be obvious from the diagram below that the great manufacturing countries have maintained the quantities of their imports better than those of their exports.

Imports and Exports of Certain Countries.
Quantum (Base : 1929 = 100).



This fact is, of course, the corollary of movements in the terms of trade by which, at least till the middle of 1932, the prices of raw materials and foodstuffs fell relatively faster than those of manufactured goods, so that, in the agricultural countries,

export prices fell relatively to import prices, and, in the manufacturing countries, import prices fell relatively to export prices. In other words, the manufacturing countries sold less but at relatively favourable prices, while the agricultural countries sold more but at very low prices. The movements of the terms of trade adversely to the agricultural countries until the middle of 1932 is clearly shown in the diagram and table in Chapter II.

Net Balance of Commodity Trade.

(+ : Excess of exports over imports ;

— : excess of imports over exports.)

Gold \$ (000,000's).

	1929		1930		1931		1932		1933
	I-VI	VII-XII	I-VI	VII-XII	I-VI	VII-XII	I-VI	VII-XII	I-VI
<i>Debtors :</i>									
Argentine . .	+113	— 26	— 32	— 72	+ 30	+ 49	+ 90	+ 25	+ 23 ¹
Australia . .	+ 15	—129	— 54	+ 12	+ 68	+ 50	+ 61	+ 20	+ 50
Austria . . .	— 72	— 79	— 64	— 56	— 62	— 60	— 52	— 36	— 29
Germany ² . .	—154	— 16	+ 32	+191	+170	+414	+128	+114	+ 68
India	+131	+131	+128	+105	+ 30	+ 61	+ 1	+ 3	+ 28
New Zealand	+ 71	— 45	+ 30	— 30	+ 34	— 3	+ 27	+ 4	+ 34
<i>Creditors :</i>									
Belgium . . .	— 40	— 64	— 90	— 46	— 16	— 1	— 16	— 25	— 13
France	—225	— 92	—166	—213	—271	—190	—205	—193	—240
Netherlands.	—143	—163	—158	—123	—125	—109	—105	— 78	— 84
Switzerland ³	— 56	— 73	— 73	—103	— 76	— 78	— 95	— 91	— 73
United Kingdom.	—903	—955	—906	—974	—885	—928	—515	—486	—411
United States . .	+347	+471	+224	+443	+196	+ 94	+ 78	+169	+ 71

The cumulative effects of the depression and of the trade restrictions which it engendered are clearly revealed both in the decreased passive balances of the creditor countries in 1932 and in the decreased active balances of those debtor countries most affected by the trade restrictions. The moral is pointed by the contrast afforded by those debtor agricultural countries which supplied markets, such as the United Kingdom and the United States, where quantitative import restrictions are not greatly developed. In such countries as Australia, New Zealand and the Argentine, the balances of commodity trade went far to right themselves by the end of 1932, and the early months of 1933 saw a considerable revival of imports into those countries. The recovery of purchasing power in these countries where the depression began so early is a good omen.

¹ January to April only. The figure for the same period in 1932 was + 68.

² Excluding reparations in kind.

³ Including bullion.

Imports and Exports of Certain Agricultural Countries.
Gold \$ (000'000's).

Country		1929	1930	1931	1932	First six months	
						1932	1933
Argentina :	Imports .	820	617	349	215	72 ¹	75 ¹
	Exports .	907	513	428	330	140 ¹	98 ¹
	Balance .	+ 87	- 104	+ 79	+ 115	+ 68	+ 23
Australia :	Imports .	706	460	197	187	79	85
	Exports .	592	418	315	268	140	135
	Balance .	- 114	- 42	+ 118	+ 81	+ 61	+ 50
Brazil :	Imports .	422	261	140	106	44 ²	61 ²
	Exports .	461	318	241	179	83 ²	82 ²
	Balance .	+ 39	+ 57	+ 101	+ 73	+ 39	+ 21
New Zealand :	Imports .	233	204	110	78	36	33
	Exports .	259	204	141	109	68	67
	Balance .	+ 26	± 0	+ 31	+ 31	+ 32	+ 34
Palestine :	Imports .	35	34	27	27	5 ³	8 ³
	Exports .	8	9	7	8	5 ³	6 ³
	Balance .	- 27	- 25	- 20	- 19	± 0	- 2
Siam :	Imports .	86	65	40	29	14 ²	9 ²
	Exports .	94	69	49	45	20 ²	12 ²
	Balance .	+ 8	+ 4	+ 9	+ 16	+ 6	+ 3
South Africa :	Imports .	417	324	263	168	74	71
	Exports .	454	389	333	322	159	155
	Balance .	+ 37	+ 65	+ 70	+ 154	+ 85	+ 84

THE CIRCULATION OF CAPITAL.

During the course of the depression, great changes have taken place in the invisible imports and exports which must be included in any complete statement of the balances of international payments.⁴ Generally speaking, these invisible items have shrunk very considerably in 1932. Thus, the external balances of the United Kingdom in respect of shipping income, income from overseas investments and net receipts from short interest and commissions have all fallen heavily.

¹ First four months.

² First five months.

³ First three months.

⁴ Cf. the forthcoming volume *Balances of Payments, 1932*, to be published at the end of 1933.

Balances of Income and Expenditure in the Transactions (other than Lending and Repayment of Capital) between the United Kingdom and all Other Countries.

£ sterling (000'000's).

	1929	1930	1931	1932
Excess of merchandise imports (including silver coin and bullion)	381	386	408	289
Estimated excess of Government receipts from overseas ¹	24	19	14	— 25*
Estimated net national shipping income	130	105	80	70
Estimated net income from overseas investments	250	220	170	140
Estimated net receipts from short interest and commissions	65	55	30	30
Estimated net receipts from other sources	15	15	10	15

Examples might be drawn from other countries. Thus, the tourist expenditure abroad by citizens of the United States fell from \$868 million in 1929 to \$446 million in 1932. Emigrants' remittances in the same period fell from \$240 million to \$138 million, and missionary and charitable contributions from \$49 million to \$31 million. The earnings of Canadians employed in the United States fell from \$13.7 million in 1929 to \$0.8 million in 1932. Dividends and trade profits remitted from the Dutch East Indies amounted, in 1929, to \$100 million, but, in 1932, had fallen to \$12.5 million. The expenses of Norwegian whaling companies abroad fell from \$5.3 million in 1929 and \$8.6 million in 1930 to \$1.4 million in 1932. While this is the general rule, there are many contrary cases where the dislocation of equilibrium between national price-levels has caused considerable shifts and, in many countries, increases in international services. Thus, tourist traffic in the gold-standard countries has fallen off; but, in the countries with depreciated currencies or with blocked accounts that can be drawn upon at favourable rates, tourist traffic has increased.

¹ Including some items on loan account.

* Estimated excess of Government payments made overseas.

*International Capital Movements.*¹
 Net Inward (+) or Outward (—) Capital Balances
 in Gold \$ (000,000's).

Country	Nature of estimate	1928	1929	1930	1931	1932
Creditor countries :						
France ²	Indirect	— 237	+ 20	+ 252	+ 788	...
Sweden	Indirect	— 19	+ 71	— 26	+ 23	...
	Direct	— 39	— 26	+ 84	+ 13	...
United Kingdom ³	Indirect	— 569	— 574	— 112	+ 313	+ 260
United States	Indirect	— 1,126	— 225	— 295	± 0	— 547
	Direct	— 1,032	— 134	— 687	— 165	— 661
Debtor countries :						
Argentina ⁵	Indirect	+ 181	+ 4	+ 243	— 27	...
	Direct	+ 131	+ 38	+ 167	+ 1	...
Australia ⁶	Indirect	...	+ 188	+ 214	+ 15	— 56
	Direct . . . . .	...	+ 99	+ 189	+ 22	— 101
Canada	Indirect	— 201	+ 65	+ 159	— 27	— 64
Denmark	Indirect	— 1	— 9	+ 5	+ 12	— 16
	Direct	± 0	— 9	+ 2	+ 29	— 18
Dutch East Indies ⁷	Indirect	± 0	+ 66	+ 60	+ 28	— 4
	Direct	— 8	+ 32	+ 32	+ 32	+ 47
Finland	Indirect	+ 40	+ 12	— 5	— 24	...
Germany ⁸	Indirect	+ 961	+ 506	+ 110	— 510	— 101
Hungary	Indirect	+ 91	+ 38	+ 24	+ 39	...
	Direct	+ 88	+ 36	+ 37	+ 50	...
India	Indirect	+ 67	+ 37	+ 92	— 86	— 25
	Direct	— 5	+ 53	+ 49	+ 4	...
New Zealand ⁹	Indirect	+ 33	+ 10	+ 29	+ 27	— 5
	Direct	+ 33	+ 14	+ 37	+ 25	— 12
Poland	Indirect	+ 124	+ 67	+ 9	+ 1	...
Turkey	Indirect	+ 11	+ 50	— 6	+ 3	...

¹ The figures are based on official or private statements concerning the balance of payments of the countries in question. Full details of the statements for the years 1927-1930 are given in *Balances of Payments, 1930* (Series of Publications 1931.II.A.28.ii).

All the figures are estimates, subject to some margin of error. Whenever possible, two figures for the capital balance are given — namely :

(1) The balance as calculated *indirectly* from the balance of non-capital items (trade in goods, gold movements, net receipts or payments on account of interest, dividends, freights, emigrants, remittances, tourists and miscellaneous services) ;

(2) The balance as calculated *directly* from the known movement of capital in the form of the new loans raised, amortisation payments, purchases and sales of outstanding securities, changes in floating debts or assets, etc. .

If the statements could be made exact and complete, the two estimates would agree exactly in each year.

When not otherwise indicated in the footnotes, payments for the amortisation of war debts, but not reparation payments, have been counted as capital items. Changes in the amount of gold under earmark held for foreign account in the country, or for national account abroad, have been counted as capital items.

[Footnotes 2 to 9 on following page.]

Such scattered illustrations as those given above serve to show in what varied directions the depression has reduced earnings and commissions. It should be noted, however, both in respect of these figures and of those quoted elsewhere in discussions of the balances of payments, that their reduction, for convenience, to gold dollar values tends to exaggerate the extent to which the shrinkage of the balances implies difficulty in meeting international financial obligations. As was previously noted in the chapter on indebtedness, the depreciation of both sterling and the dollar from their gold parities has greatly relieved the external burden upon those countries whose debts are expressed in terms of the depreciated currencies.

The striking extent to which normal capital movements have been reversed in recent years may be illustrated by the preceding table and the diagram which follows. It will be seen that there is a clear tendency for the great creditor countries to receive net imports instead of sending out net exports on capital account, while the debtor countries have a net export balance on capital account.

The reversal of capital movements in recent years is obviously due to the fact that debtor countries have continued to pay interest and amortisation, except where there has been a flight of capital or where excessive strain on their external balances has caused them either to default or to seek temporary accommodation from their creditors, while new capital issues on foreign account in the great financial centres have shrunk very greatly indeed. Defaults and suspensions of transfer have been responsible for some of the shrinkage of invisible imports and exports previously referred to. Thus, it is estimated that the net income received in the United Kingdom from overseas investment suffered the following changes in 1931: defaults on overseas Government loans amounted to £1,000,000, while the interest receipts from other loan capital fell by about 10 per cent and receipts from variable interest securities (including preference shares) fell by 40 per cent. In 1932, defaults on Government loans amounted to £5,000,000; but interest receipts on other loan capital kept up fairly well, the defaults which occurred being largely offset by the

‡ Excluding amortisation of inter-allied debts.

* Excluding Government capital transactions (*e.g.*, receipts and payments on account of war debts).

^ (1932) Of which net release of gold from earmark — 457.

* Year ending September 30th. Excluding amortisation of public debt and certain mortgage bonds.

* Year ending June 30th.

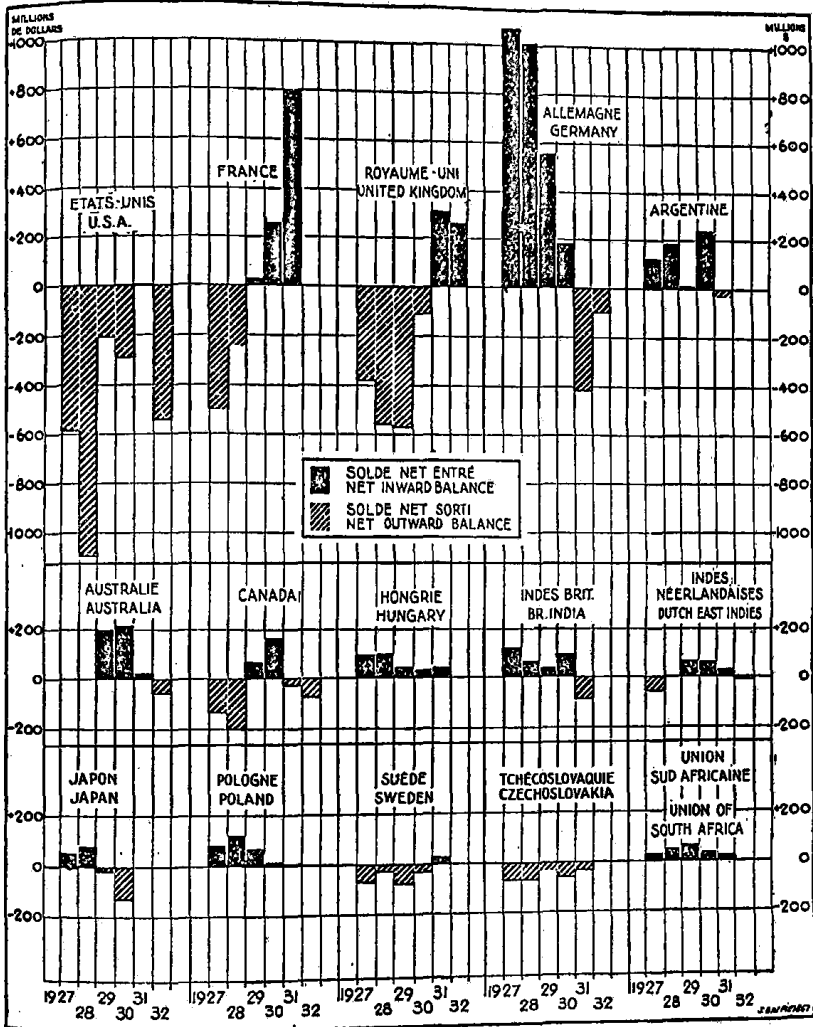
* Excluding re-investment in the country of interest and dividends earned by foreign capital.

* Excluding amortisation of the Dawes Loan (about \$6 million annually).

* Year ending March 31st of following year.

International Capital Movements. ¹

Net Inward (+) or Outward (—) Balances in Terms of Gold \$ (000,000's).



¹ Cf. League of Nations *Monthly Bulletin of Statistics*, No. 5, May 1933.

gold premiums on some payments. The returns on variable interest securities, however, fell off one-third from the 1931 total.

The extent to which international lending has shrunk is disclosed in the following table :

*Issues for Foreign Account.*¹
\$ (000,000's).

In		Europe	Asia and Oceania	Africa	Canada and Newfoundland	Latin America	Issues not specified	Total
United States of America	1928	598	137	—	185	331	—	1,251
	1929	142	58	—	295	176	—	671
	1930	233	62	—	281	199	130	905
	1931	78	25	—	125	1	—	229
	1932	—	—	—	29	—	—	29
United Kingdom	1928	164	232	80	98	96	28	698
	1929	105	139	51	74	78	12	459
	1930	53	195	129	17	101	34	529
	1931	14	125	36	6	26	2	209
	1932	—	40	46	9	—	7	102

It is quite clear also that, together with this great shrinkage of foreign lending, the tendency noted in the *Survey* for 1931-32, for such lending to be confined mainly to Government loans in countries connected closely with the lending centre, has been strongly accentuated. For example, the total issues on foreign account in the London Money Market amounted, in 1929, to £94,300,000 and, in 1932, to £29,200,000. Government loans declined from £30,400,000 to £24,600,000 ; municipal issues from £4,300,000 to £1,000,000 ; railway loans from £12,300,000 to £1,300,000 ; and loans for industrial undertakings from £47,300,000 to £2,300,000. It is particularly significant that, whereas loans to India and Ceylon declined in these years from £10,100,000 to £6,400,000, and those to other British countries from £44,300,000 to £22,500,000, loans to foreign countries, mainly because of the embargo imposed during the conversion period, ceased almost completely, falling from £39,900,000 to £300,000.

The liquidation of short-term balances during the latter half of 1932, already referred to in Chapter VIII, was not as great

¹ League of Nations *Balances of Payments, 1931-32*. The figures for the United States refer to nominal value, and those for the United Kingdom to price of issue.

as that which took place in the twelve months after the financial panic set in during the spring of 1931; but, as in 1931, this movement reinforced the drain of capital upon many debtor countries. The net results may be roughly summarised in the following table:

*International Short-Term Capital Movements.*¹
Inward (+) or Outward (—) Capital Balance in Millions of Dollars,
based on Direct Estimate of Changes in Floating Debts
or Assets.

	1927	1928	1929	1930	1931	1932
<i>Creditor countries:</i>						
Sweden ²	— 54	+ 10	— 18	+ 8	+ 48	...
United States	+ 1,005	— 348	— 40	— 463	— 398	— 908
<i>Debtor countries:</i>						
Argentina	— 8	+ 24	— 11	— 8	+ 7	...
Czechoslovakia	— 13	— 12	+ 4	— 28	+ 35	...
Denmark	— 28	— 42	— 3	+ 5	+ 35	— 11
Germany (incomplete data)	+ 634	+ 536	+ 349	— 156	— 553	— 56
Hungary ³	+ 35	+ 33	— 2	+ 2	+ 47	...
Norway	— 14	— 13	+ 18	+ 41	+ 19	— 13

Such a stoppage, and in many cases reversal, of capital movements gravely affected the terms of trade in the debtor countries; but, as was previously indicated, the more favourable price movements in the latter part of 1932, combined with considerable measures of internal adjustment in the debtor countries, placed many of them in a somewhat more favourable position at the end of the year. The violence of the price movements and of exchange rates in 1931 and the early part of 1932, together with the restrictions on trade and foreign exchange controls, distorted the normal relationships to a degree that can be described only as a destruction of international economic equilibrium. The connection between capital exports, gold movements, the relative prices of raw materials and finished products, and industrial activity demonstrated in the preceding *Survey*⁴ was temporarily obscured by the violence of price movements and the collapse of economic activity in the financial panic.

¹ League of Nations *Monthly Bulletin*, No. 5, 1933. The footnotes to the table on international capital movements apply also to this table.

² Operations by banks only.

³ In the years 1930 and 1931, medium-term capital transactions are included.

⁴ Page 184.

Brief reference should be made, in conclusion, to the far-reaching effects of the decisions recently taken in the United States and the United Kingdom concerning the legal validity of the "gold clause" in debt contracts. Such clauses, stipulating in various formulæ the payment of interest and amortisation in gold currency of a specific standard weight and fineness or in gold currency of the standard in force at a particular date, were commonly incorporated in loan contracts mainly as a guarantee to the lender against losses entailed by currency depreciation. Apart, however, from depreciation, price movements entailed some element of uncertainty in the commodity value of payments spread over a long term of years. Rising prices entailed some loss to creditors; falling prices some gain. In recent years, the fall in prices has been so severe that a considerable extra strain was placed upon the debtors required to pay in currencies which had appreciated violently.

As one result of the measures taken to deal with the banking panic, and of the depreciation of the dollar, legislation abrogating the gold clause was passed in the United States. The law of March 14th, 1900, defining the dollar of 25.8 grains of gold, nine-tenths fine, as the standard currency of the United States, was repealed, and the gold clauses in existing contracts were declared invalid as "against public policy". This legislation applies to all contracts, domestic or foreign.

A decision of the British Court of Appeal in a case brought by a bondholder to secure enforcement of the gold clause in a loan contract upheld the decision of the Court of Chancery that payment in legal tender satisfied the debt. It was held invalid for the contracting parties to assess consideration to be paid in terms of a currency not recognised by the State as legal tender.¹

In the same sense, the action of the British Treasury in paying the obligations due under a 5½ per cent dollar loan in paper dollars, though partly compensated by a conversion offer which gave favourable terms to the holders of the loan, was a *de facto* recognition of the validity of the United States action in abrogating the gold clause in existing contracts.²

The highest courts — the Supreme Court of the United States and the House of Lords — have not yet pronounced on this issue, so that the legal position remains somewhat in doubt. If the decisions are upheld, they clearly affect very considerably the prospects of a resumption of international capital movements in the future, and may cause important changes in the form which any such capital movements take.

¹ *Cl. Economist*, March 25th, 1933, page 647.

² *Ibid.* July 22nd, 1933, page 175.

GOLD MOVEMENTS DURING 1932.

The main interest attaching to gold movements since the financial panic which began in the spring of 1931 has lain in their bearing upon the distribution of gold reserves in the world, and not in their bearing upon the balancing of payments. The breakdown of the gold standard has dissociated gold shipments from current requirements on trading account. Such international economic equilibrium as exists has been secured by changing price-levels and fluctuating exchange rates with which the gold movements have had little connection.

The fact that in 1932 "gold movements reached proportions never before experienced" is, however, sufficient evidence of the great importance still attached almost universally to the possession of gold. By a gradual process of evolution extending over many centuries, it has become recognised as a standard of value, and it is clear that the value of gold in terms of commodities is largely derived from the monetary demand, which is much greater than the demand for its use in the arts or for ornament. There is quite obviously a widespread expectation that gold will continue to be used for monetary purposes, and possibly at higher commodity values resulting from currency devaluation in many countries. The competition for gold has been greater and the price paid for it has been higher since its use as a standard of value was suspended in so many countries, and this can only be in anticipation of the resumption of the gold standard at a future date.

During 1932, the production of new gold from the mines reached record figures, the increase being widespread, but greatest in South Africa, Canada and the United States.¹ The search for gold, especially in the countries which, by departing from the gold standard, have raised the price of gold in legal tender, has been one of the picturesque results of the depression. The greatest practical effect has been the increase of the ore mined by large-scale capitalist methods. Low-grade and deep ores, which were not profitable at the price ruling before the abandonment of the gold standard, became profitable when the standard was abandoned. Prospecting for new goldfields was also pushed energetically in widely separated countries — in Siberia and the Soviet Union, Australia and New Zealand, Japan, Canada and Kenya — and old fields were worked over once more by new methods.

¹ In 1933, however, as the export of gold is prohibited and there is no free gold market, production in the United States has fallen substantially. The domestic output of gold fell from 252,000 fine ounces in March to 189,000 in April, 185,000 in May and 142,000 in June. *Annalist*, August 4th, 1933.

The result of all this activity is summarised statistically in the following table :

The Production of Gold.¹
(Kilogrammes.)

	1929	1930	1931	1932
South Africa	323,860	333,316	338,337	359,504
Canada	59,977	65,382	83,789	94,884
United States ²	64,042	66,521	68,854*	70,894*
Australia	13,286	14,513	18,745	22,000*
Mexico	20,276	20,808	19,378	18,164
Southern Rhodesia	17,443	17,033	16,551	17,858
Japan	10,422	12,068	13,372	13,200*
India	11,315	10,239	10,280	10,000
Belgian Congo ³	5,375	6,093	7,425	8,547
Gold Coast	6,465	7,493	8,138	...
Colombia ⁴	4,248	4,937	6,043	7,721
Philippines	4,996	5,574	5,400	7,100
New Zealand	3,500	4,015	4,045	6,200
Korea (Chosen)	5,553	6,186	9,031	6,000
Other countries (approx.)	28,000	28,500	30,000	32,000
Total	579,000*	603,000*	639,000*	683,000*

Another result of the gold premium in terms of depreciated currencies has been the release of unexpectedly large amounts of gold from hoards in Far-Eastern countries. The amount of gold thus made available from India alone is estimated by the Bank for International Settlements as amounting during 1932 to "more than 1,000 million Swiss francs, a sum not greatly inferior to the value of South-African production, which was 1,238 million Swiss francs".⁵

The greater amounts of gold made available have been absorbed mainly in Central Bank monetary reserves. The demand for gold in the arts has fallen to very low levels, and, with the normal flow of gold to the Far East for hoarding reversed, much greater amounts were available for monetary purposes. Hoarding in certain European countries, and for a time in the

* Provisional.

¹ League of Nations *Statistical Year-Book, 1932-33*, page 130. The data represent, wherever possible, the fine-gold content of ore mined or exported. For a certain number of countries, however, the data represent smelter production. In several cases, the original data do not contain any reference to the nature of the statistics. The world totals are affected by the exclusion of China and the U.S.S.R. and by the uncertain character of the statistics of several South-American countries.

² Including Alaska.

³ Industrial production.

⁴ The data are uncertain and vary.

⁵ "Third Annual Report", *cf. cit.*, page 6.

United States, caused a drain upon these reserves ; but at the middle of 1932 they stood at higher levels than any previously recorded. The following table shows, however, that very great changes took place during the period 1931-1933 in the holdings of individual Central Banks. In the previous *Survey*, a diagram was presented showing the movement of gold reserves of Central Banks and Treasuries from 1925 to March 1931. The table and diagrams which follow supplement this diagram by showing quarterly movements since that date.

Central Monetary Gold Reserves of the World at End of Successive Quarters.
Gold \$ (000,000's).

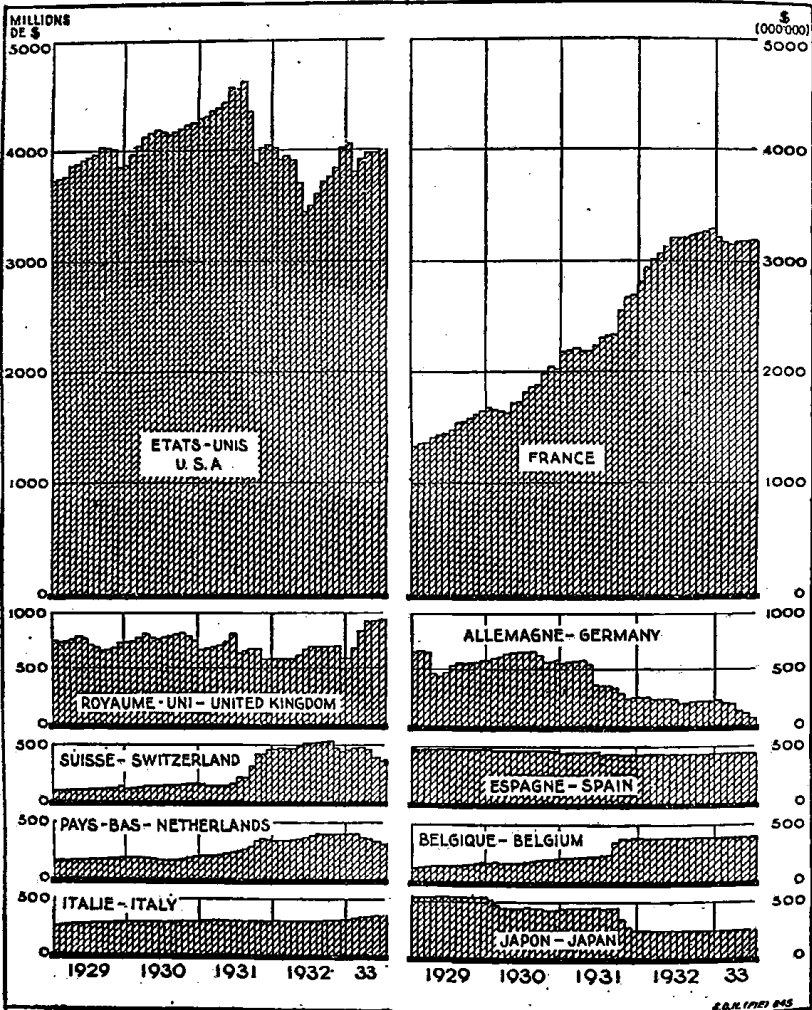
Country	1931			1932				1933	
	II	III	IV	I	II	III	IV	I	II
United States	4,593	4,365	4,051	3,986	3,466	3,748	4,045	3,916	3,996*
France	2,211	2,325	2,683	3,010	3,217	3,239	3,257	3,150	3,183
United Kingdom and Irish Free State	800	662	590	591	666	683	587	840	927
Spain	468	439	434	434	435	435	436	436	436
Belgium	200	347	354	350	357	359	361	371	372
Switzerland	162	328	453	471	503	509	477	489	361
Italy	283	287	296	296	298	305	307	331	356
Netherlands	200	282	357	353	394	416	415	381	309
Argentina	349	279	252	248	248	248	248	248	248
Japan	424	408	234	214	214	214	212	212	212
India	151	162	162	162	162	162	162	162	162
Sweden	64	53	55	55	55	55	55	62	71
Germany	354	326	251	226	215	207	209	193	62
Poland	64	64	67	64	54	55	56	55	53
South Africa	36	36	43	36	42	35	39	55	71
Czechoslovakia	46	45	49	49	49	49	51	51	51
Other countries									
World Total (excluding U.S.S.R.).	11,130	11,102	11,052	11,262	11,092	11,427	11,632	11,667	11,580*

The movements that have taken place are shown graphically in the following diagrams, which make clear the successive losses, alternating with partial regaining of reserves, in the United States ; the stabilisation of French holdings after a rapid increase till the middle of 1932 ; the steady growth of the Italian reserves ; the strengthening of the British position in 1933 ; the weakening of those in Germany and Japan, and the substantial increases in Switzerland, Belgium and the Netherlands in 1931 and the early part of 1932.

It remains only to draw attention to the development on a great scale of gold hoarding in various Western countries, particularly in Western Europe and the United States of America. A gradual concentration of the gold stocks of the world into Central Bank reserves was taking place up till about the middle of 1931 ; but at that time fears of currency instability, dramatically

confirmed by the depreciation of sterling in September, led to hoarding on a large scale. In spite of a decline in the industrial consumption of new gold and a considerable increase in world gold production, and although very important amounts of gold from Indian hoards and other non-monetary sources became available for monetary use, total central gold reserves actually dropped between the end of June and the end of December 1931.

Central Monetary Gold Reserves of Certain Countries.
In Terms of Gold \$ (000,000's).



Although total reserves again increased very considerably in the course of 1932, this increase fell appreciably short of the total of new gold and old non-monetary gold which in that year became available for monetary purposes. On the basis of such information — in part, rather approximate in character — as is available concerning gold production, consumption in the arts and releases from old non-monetary gold stocks, it may be indirectly estimated that the total "other monetary gold stocks", which in June 1931 was about \$700 million, had increased at the end of 1932 to roughly \$1,250 to \$1,300 million, mainly on account of private hoarding in Europe and North America.

In the first half of 1933, there was a further development of private hoarding in certain parts of the world. After the banking panic in the United States, legislative action was taken to compel a return of hoarded gold to bank reserves; but hoarding in Europe continued, and is still in progress at the moment of writing.

Chapter XI.

THE ECONOMIC SITUATION IN JULY 1933.

THE MONETARY AND ECONOMIC CONFERENCE.

The statistical evidence of rising prices, increased production and diminished unemployment presented in the succeeding sections of this chapter indicate that, in the second quarter of 1933, there was, at least temporarily, a definite upward turn in the business cycle. The fact that this improvement followed a similar period of revival in the third quarter of 1932, not all of which was lost in the winter recession, encouraged the belief that a measure of adjustment had taken place in a sufficiently large number of countries to warrant the hope that the period of deflation and deferred business activity was working itself out. Large problems remained to be solved, and some of them, notably the paralysis of international finance, exchange instability, and the widespread and drastic restrictions imposed on international trade, threatened to set fairly narrow limits, both in extent and in time, to the recovery which appeared to be under way. These obstacles lay almost entirely in the sphere of international action, and there was general agreement that steps towards their removal were essential if recovery was to be lasting and substantial.

It was to take the necessary measures in these fields that the Monetary and Economic Conference was decided upon at the Lausanne Conference in July 1932; but it was recognised that the timing of the Conference presented a delicate and difficult problem. The Preparatory Commission of Experts, which in January 1933 worked out the Draft Annotated Agenda for the Conference, represented the need for action as urgent; but, before the Conference was convoked, the economic situation had greatly changed. The actual date for the opening was decided by the Organising Committee as a result of conversations held at Washington late in April between the President of the

United States and visiting statesmen, including the Prime Minister of the United Kingdom, who was President-elect of the Conference.

The date chosen was June 12th, 1933, and the Conference was duly opened at that time by His Majesty King George V. Sixty-four Governments sent delegations; but the general debate with which the proceedings were opened was concluded within three days. During those days, negotiations on the war-debt payments were in progress outside the Conference. On June 15th, the United States accepted token payments from a number of countries, including the United Kingdom, payment was made in full by Finland, and no payments were made by the other debtors.

The Conference approached the detailed consideration of its problems by setting up plenary commissions to deal respectively with economic and with financial questions. The Economic Commission, after a general discussion of the subjects on its agenda, divided its work into four main groups, dealing respectively with Commercial Policy, Co-ordination of Production and Marketing, Indirect Protection and Public Works. Sub-committees were set up to deal with the first three of these groups, while the last was discussed briefly in the Commission itself.

The Conference had been preceded by a tariff truce initiated on the proposal of the United States Government at the meeting of the Organising Committee which definitely convoked the Conference for June 12th. The Governments represented on that Committee adhered to the proposal with some reservations in particular cases, including the right to use tariff policy as a defence against exchange dumping from countries with depreciated currencies. In the early stages of the Conference, further adhesions were secured from virtually all the countries represented.¹ The truce bound the contracting parties to refrain from new tariff initiatives for the duration of the Conference, or, if it lasted after this date, until the end of July 1933, when the agreement might be terminated by one month's notice.

The Conference Committee on Commercial Policy, after general discussion of the two main problems presented to it — viz., the abolition of quantitative restrictions on imports and tariff policy, including the most-favoured-nation clause — became involved in the conflict of policies which arose in connection with currency stabilisation. The hypothesis upon which discussion had proceeded had been that currencies would shortly

¹ *Monthly Summary of the League of Nations*, Vol. XIII, No. 5, page 106, and Vol. XIII, No. 6, June 1933, pages 110 and 111; also *League of Nations Journal of the Monetary and Economic Conference*, London, 1933, No. 39, July 28th, 1933.

be stabilised, at least by a *de facto* arrangement. When it became clear that this hypothesis could not be realised immediately, several countries felt it necessary to reserve full liberty of action in regard to quantitative restrictions, exchange control and Customs tariffs. While other countries were prepared to take part in drawing up a constructive programme to be put into effect when currency stability had been achieved, it was not found possible to do more than register the measure of agreement that had tentatively been reached and the divergent views expressed upon methods by which trade restrictions might be removed or modified.¹

Greater progress was made in the sub-committees which dealt with various forms of indirect protectionism. A resolution was passed recommending, in regard to indirect protectionism in general, that a clause should in future be inserted in commercial treaties stipulating that, if either party to the treaty considers any new practice (other than Customs tariffs or questions specifically settled in the treaty) to nullify or impair the object of the treaty, the other party shall not refuse to negotiate on this question.² It was further recommended that the attention of Governments should be drawn to the Convention of November 3rd, 1923, concerning the simplification of Customs formalities, and the opinion was expressed that the work of the Economic Committee of the League of Nations was sufficiently advanced in regard to many of these questions to warrant the convening of a special conference at an appropriate date.

The technical problems relating to veterinary and phytopathological regulations, which act as restrictions on imports, were also advanced a stage nearer solution. The Committee which considered this subject recommended that the Council of the League of Nations, at its next session, should convene a diplomatic conference to arrive at a new Convention regarding animal products. It referred the scientific and technical questions involved in regulating the import and export of plants and other vegetable products to the International Institute of Agriculture for further study. The principle was asserted, in this connection also, of international consultation before the application of new trade restrictions.³

Substantial disagreement prevented the adoption of unanimous recommendations regarding either the problems raised by the growing practice of requiring marks of origin, or the questions of subsidies and bounties. The committees on these questions

¹ League of Nations: Monetary and Economic Conference, "Report of the Bureau to the Conference", London, July 26th, 1933 (Conf.M.E.22), pages 22-24.

² *Ibid.*, page 30.

³ Report, *op. cit.*, page 31.

therefore merely recorded the points upon which agreement had been reached and those upon which it had been impossible to reconcile divergent views. The proposals submitted to the Economic Commission by the International Labour Organisation recommending consideration of an international programme of public works were the subject of a brief discussion, in which divergent views were stated, but were not examined in detail.

The remaining group of subjects relating to the co-ordination of production and marketing came to occupy a prominent place in the deliberations of the Conference. In the early stages of its work, the Sub-Committee established agreement upon certain general principles to which it was considered desirable that any agreements to co-ordinate production and marketing of particular commodities should conform.¹ Those principles, while drawn in general terms, in effect confine the possibilities of agreement to a limited number of raw-material commodities and foodstuffs of wide usage. Smaller committees of experts were set up to consider dairy products, sugar, wine, coffee, cocoa, timber, coal, copper and tin, while negotiations which had been proceeding among experts representing the chief wheat-exporting countries were continued during the Conference period and were extended to conversations with other wheat-producing countries as well as importing countries. Definite agreement was not reached in any of these committees; but it was noticeable that a strong tendency developed to support the work already being accomplished in the field of international regulation of production and marketing by such bodies as the International Sugar Council, the International Wine Office and the International Tin Commission. There was division of opinion, however, as to the desirability, in normal times, of agreements to regulate production and trade, and, while it was agreed that exceptional circumstances might call for such measures, several delegations insisted on the necessity of avoiding anything which might give the impression that the regulation of production could be defended except as a temporary expedient employed in abnormal circumstances.²

On the economic side of the Conference, therefore, while some progress was made in exploration of the practical difficulties involved both in the reduction of trade barriers and in the co-ordination of production and marketing, definite agreements were not reached except in preparatory fields. In the closing days of the Conference, the United States delegation communicated a detailed programme for further committee work during the

¹ Report, *op. cit.*, pages 19 and 20.

² *Ibid.*, page 18.

adjournment of the full Conference upon a series of detailed problems in the field of commercial policy.¹

The Monetary Commission divided its work between two sub-commissions. The first dealt with "Immediate Measures for Financial Reconstruction", including credit policy, price-levels, the limitation of monetary fluctuations, exchange control, indebtedness, and the resumption of international lending. The second dealt with "Permanent Measures for the Re-establishment of an International Monetary Standard".

The second of these sub-commissions proceeded immediately to pass two resolutions to the effect that "stability in the international monetary field be attained as quickly as practicable" and that "gold should be re-established as the international measure of exchange values, time and parity being for each country to determine". These resolutions were later supplemented by two others stressing the undesirability of using gold for internal circulation and advocating the reduction of legal minimum gold reserves, where the system of reserve ratios as cover for Central Bank liabilities is in force.² The two latter resolutions were passed upon the recommendation of an expert Sub-Committee set up to consider technical monetary problems connected with the working of the gold standard. As a result of further recommendations by the same Sub-Committee, other resolutions were passed, advocating the establishment of Central Banks in developed countries where they do not now exist, re-affirming the great utility of close and continuous co-operation between Central Banks and the important rôle in that respect of the Bank for International Settlements, and recommending those agricultural countries which desire advice upon the adaptation of their Central Banks to their special needs to consult the appropriate international organisations specially competent to advise on such matters. The Sub-Committee further considered a statement of general principles of Central Bank monetary policy, but did not recommend it for adoption as a resolution of the Conference, though it was agreed by all the Governments represented on the Sub-Committee, with the exception of that of the United States, which considered discussion of this subject premature, it being understood that the Federal Reserve Banks would be glad to confer at an opportune time with other Central Banks on questions of this character to the extent that they are compatible with national policies.³

Another sub-committee, composed of representatives of

¹ Report, *op. cit.*, pages 41-43.

² *Ibid.*, page 12.

³ *Ibid.*, pages 13 and 14.

silver-producing countries and of countries holding large silver stocks, recommended a resolution, which was adopted, aiming at the stabilisation of the market for silver. This resolution was implemented during the course of the Conference by a definite agreement signed by the principal countries concerned. The chief provisions of this agreement were an undertaking by the Governments holding large silver stocks to confine their sales within a maximum agreed figure for the next five years and a similar undertaking by the Governments of the producing countries to purchase amounts of silver which would offset such sales. These provisions, supplemented by others in which all the Governments undertook in principle to refrain from debasing their silver coinages, had for their object the freeing of the market from the disturbing sales of large quantities of demonetised silver.

The first Monetary Sub-Commission, dealing with "Immediate Measures of Financial Reconstruction", began its work by a general debate on credit policy and price-levels. While this debate was in progress, however, in the latter part of June, the fluctuations of the dollar exchange became greater and, in the early part of July, the rate rapidly approached parity with sterling. The fluctuations of the dollar which began in the second half of April came after a period of several months, during which the major currencies of the world had been relatively stable. Sterling, for example, had, since February 1933, maintained a fairly steady relationship with the gold currencies, and a great number of other currencies had maintained a stable relationship with sterling. The depreciation of the dollar therefore introduced a new and disturbing element, which was recognised in the official statements issued when the Conference was convened. At that time, exchange stabilisation was recognised as one of the major problems confronting the Conference.

By the time the Conference opened, the dollar, after falling in mid-April 10 per cent from its gold parity and remaining about that level till the end of the month, had, with some fluctuations, drifted lower, until its external value was 20 per cent below gold parity. Negotiations which took place independently of the Conference appeared to offer some prospect of early *de facto* stabilisation, and the exchange rose slightly in the middle of June; but the breakdown of these negotiations led to renewed weakness, and by the middle of July the dollar touched parity with sterling for the first time since September 1931.

In face of these movements, which were accompanied by unusually wide fluctuations from day to day, the problem of exchange stabilisation was regarded by many of the delegations

as the most immediate and urgent task before the Conference. In published statements, however, the United States Government made it clear that the development of its domestic programme of industrial re-organisation and other measures designed to raise prices made impossible any commitment at the moment concerning stabilisation of the dollar exchange. When it became clear that there was no immediate prospect either of currency stabilisation by controlling the fluctuations of the dollar relatively to the gold currencies and sterling or of an international agreement whereby the other countries would join the United States in a policy aimed at raising prices, the proceedings of the first Monetary Sub-Commission reached a deadlock.¹ Subsequently, discussions were confined to the problem of indebtedness, concerning which the resolution was passed which has been referred to in a preceding chapter.²

The Conference held the final meeting of its first sessions on July 28th. The reports of the Monetary and Economic Commissions were adopted in plenary session and a resolution was passed authorising the Bureau to take whatever action it considered likely to promote the success of the Conference, whether by the convocation of any committee set up by the Conference or of representatives of States especially concerned in any particular problem, or by the reference to experts for study of any special question. The Bureau was also empowered to determine the date of the re-assembling of the Conference.

THE AMERICAN EXPERIMENT.

The first chapter of this *Survey* briefly summarised the outstanding economic developments between the summer of 1932 and March 1933. Subsequent chapters have, for the most part, been confined to analysing in further detail the various aspects of economic activity during that period. The general impression to be gained from such an analysis is that, while not all of the autumn recovery had been lost in the recession that set in during the winter, and while there was some evidence of a new equilibrium being achieved upon the basis of which the forces of recovery might have been expected to build, the situation in the first quarter of 1933 was precarious. The great event, which within a few weeks created a new and very different situation, was the launching and rapid development of the programme of domestic recovery in the United States. This programme, the

¹ Report, *op. cit.*, pages 9-11.

² Chapter IX. See also Report, *op. cit.*, page 11.

beginnings of which were evident as soon as the new Administration took office early in March, did not begin to take definite shape until after the abandonment of the gold standard on April 19th. After that date, very far-reaching legislation was rapidly passed, giving unparalleled powers to the Executive, so that, by the time Congress rose on June 16th, all the machinery necessary for the execution of the new plan was in existence and energetic steps were being taken to bring that machinery into practical action.

The importance of the developing plan, the main features of which are outlined below, is to be found primarily in its effect upon the domestic recovery of prices and production within the United States, and it is this aspect of the new programme of action which has engrossed most popular attention. It is obvious, however, that concentration upon domestic recovery has implied not so much the disturbance as the neglect of international economic equilibrium. The practical manifestation of this fact is seen in the fluctuation of the dollar exchange relatively both to the gold and to the sterling currencies, which, as was pointed out in an earlier chapter, had been in relatively stable equilibrium since February. Not the least important aspect of the great experiment now in process lies, therefore, in the unresolved problem, first, whether the equilibrium which was in process of being established between the gold and sterling currencies can be maintained in face of the added complications caused by the depreciation that has already taken place in the dollar, and, secondly, whether the upward impetus imparted to the American price system can endure and be transmitted to other national price systems without the necessity of further depreciation in the dollar exchange to an extent which would definitely disturb the existing currency equilibrium and force competitive depreciation of other currencies. It is obviously premature at the present time to attempt even hypothetical answers to these questions. The depreciation of the dollar is, of course, by no means the only factor to be considered. Domestic circumstances and developments in other countries, both in the gold *bloc* and in the sterling *bloc*, will exercise an important influence. The maintenance of exchange stability may, in any case, prove difficult enough, even apart from the influence exerted by the course of the dollar exchange. Time alone will show whether the methods now being utilised to force a revival of prices and economic activity in the United States will prove effective without recourse to such further monetary action as may drive down the external value of the dollar still further. Whether in the working out of the experiment the rise of prices will spread to other countries in sufficient degree to assist them in maintaining the measure

of equilibrium so far achieved until the area of stabilisation can be extended to include the United States, or whether the disturbance caused by the experiment will further complicate international economic relations, is a question the answer to which must be recorded in future *Surveys*. At the present time, when the experiment is merely in its first stages, all that can be done is to summarise the main outlines of the plan of action as revealed in the legislation passed and the administrative steps already taken, and to record the actual developments of prices and economic activity in the meantime.

Even this limited task presents difficulties. The legislation passed covers a very wide scope, and the greater part of it is permissive rather than mandatory in character. The administrative machinery so far created is, at the time of writing (July 1933), only just beginning to function. It is not possible, therefore, to state with any certainty the precise ways in which it is likely to develop, the extent to which use will be made of the wide powers entrusted to the President's discretion, or the relative emphasis which will be given to one aspect or another of the developing plan in face of circumstances and attitudes that cannot yet be clearly foreseen. In the same way, it is possible to record the latest statistics of prices, employment, wages, production, trade and other economic phenomena; but it is not possible to estimate the cause of such changes as have taken place. Economic forces work slowly and sometimes take unexpected directions. It is not yet clear how far the improvements and recessions of industry in the first weeks of the new plan's operation are due to that plan or the result of prior causes. Nor can it be expected that the forces liberated by the plan have yet produced their final or even their most important effects.

The plan, which has already passed through at least three major stages of development, is so far-reaching and has so many aspects that, in any brief summary, attention can be directed only to the salient features of the more important and overt measures already taken. Complicated details and latent possibilities must necessarily be ignored, though, in the process of development, some of these may eventually prove to be extremely important. The summary which follows is concentrated upon the domestic features of the plan, upon the assumption, which appears to be warranted by the facts, that its international aspects are, for the moment at least, regarded as secondary and have therefore been left largely to take their own course. It is obvious that, in any final estimate, the effects of the plan upon the external trade and finance of the United States must be taken into consideration; but those effects depend upon

so many factors other than those arising from the domestic situation that they must be left aside for the present. The future course of prices in other countries, the reaction upon other exchange rates, upon tariff policy and trade restrictions generally cannot yet be foreseen.

The first immediate problem with which the new Administration was faced when it took office on March 4th, 1933, was the collapse of the banking system, which culminated on that very day with the proclamation of a national bank holiday and the closing of the Stock Exchanges. The vigorous measures taken to combat this situation have already been described in Chapter VIII. Besides the Emergency Banking Act signed on March 9th, and the Banking (Glass-Steagall) Act of 1933, signed on June 16th, reference should be made to the Federal Securities Act, signed on May 27th, laying down more stringent regulations to control the issue of new securities, and the Decree of April 5th prohibiting gold-hoarding and requiring the return of hoarded gold to the banks before May 1st.

The budgetary problem also demanded attention at a very early stage, and the new Administration, working with a new and politically sympathetic Congress, was able to take swift and effective steps to reduce expenses and increase taxation so as to reduce very considerably the alarming budget deficit that appeared to be in prospect. Approximately \$500 million were saved by a 15 per cent reduction of civil service salaries and a 10 per cent reduction in the payments to war veterans, combined with more stringent administration of such payments. At the same time, the various schemes of domestic recovery summarised below called for increasing expenditure which it was planned to meet by means of new loans. The debt service on these loans, however, is to be covered by the proceeds of new taxes, mainly on individual and corporate incomes. There remained a substantial deficit,¹ involving a growing burden of floating debt. On July 31st, the Treasury invited subscriptions to a new issue of \$500 million 3¼ per cent Treasury Bonds with a currency of eight years, and \$350 million 1½ per cent Treasury Notes with a currency of two years. The prompt over-subscription of these issues, together with the extremely low rates ruling for shorter-term Treasury bills and the improvement of revenue receipts, enabled the President to claim that he had fully maintained the public credit, and that there was every reason to expect that the larger loan operations which will be necessary in the near future would be successful.

The emergency measures in respect of the banking crisis

¹ Cf. Chapter VI.

and the situation of the public finances occupied the greater share of attention for the first few weeks of the new Administration's tenure of office, and the vigorous steps taken to gain control of these difficult problems were along lines generally regarded as orthodox. The introduction of the Farm Relief Bill to Congress on March 18th initiated the more experimental measures proposed by the Administration. As these measures developed between March and July they passed through three main phases. In the first phase, emphasis was laid upon a double programme of agrarian legislation to relieve the situation of the farmers, and of positive action, mainly in the promotion of public works, to relieve unemployment. The second phase began with the imposition of an embargo on the export of gold on April 20th and the acceptance of the Thomas amendment to the Farm Relief Bill, giving the President wide powers of an inflationary character. In this phase the emphasis was laid upon monetary measures to raise prices. The third phase of the plan began early in July, after prices had risen and production had increased substantially. The dominant feature of this phase is the stress laid upon the regulation of industry under the National Industrial Recovery Act, and especially upon the effort to increase employment and raise wages. It is evident that the Administration's plans have been rapidly improvised under the pressure of urgent changing conditions.

The main features of the agrarian programme are contained in the Agricultural Adjustment Act, which incorporates the earlier Farm Relief Bill, with its proposals for contraction of acreage, and the Farm Debt (Mortgage) Relief Bill, with its provisions for the re-financing of farm debt, as well as the so-called Thomas amendment, which became the basis of the second phase of the Government's programme.

The theory of this Act is that the shrinkage of agricultural income is a primary cause of the economic depression. Power is therefore taken to issue 4½ per cent Federal Land Bonds to the amount of \$2,000 million, with the object of making mortgage loans to farmers at 5 per cent to enable them to repay existing mortgages carrying higher rates of interest.¹

The main provisions of the Act, however, are concerned with an effort to rationalise agricultural production and prices so as to improve the farmers' income and purchasing power. The Secretary of Agriculture is given discretionary power to levy a tax on the processing of farm products, to allot production

¹ The Home Owners' Loan Act, signed on June 13th, extends similar facilities to owners of house property, a further issue of 4 per cent bonds to the amount of \$2,000 million being authorised for this purpose.

quotas, fix prices, and make "rental or benefit" payments to farmers who contract to reduce their production.

The application of these powers is best described in connection with specific commodities. The processing tax levied amounts to the difference between current average farm prices and the "fair exchange value", which is defined as the 1909-1914 average purchasing power of farm products with respect to the articles farmers buy. To put the farmers in the same relative position as they enjoyed in 1909-1914, it is calculated that the prices of farm products should be 88.4 cents for wheat, 12.4 cents for cotton, 7.24 cents for hogs and 64.2 cents for maize.

The wheat processing tax was accordingly fixed at 30 cents a bushel, roughly the difference between the current price at June 15th and the standard price of 88.4 cents. The tax falls on the consumer, and the proceeds are distributed to farmers who have agreed to reduce their acreage in an agreed proportion. After the plan was launched, wheat prices rose quickly, largely on account of the comparative failure of the harvest, until the average price on farms was about 75 cents. Though later setbacks occurred, this rise in prices obviously reduced the discrepancy which it was desired to eliminate between the farmers' prospective income and expenditure. On June 21st, however, the Secretary of Agriculture strongly urged the fulfilment of the original plan, on the ground that it was necessary to take account of existing stocks and of future harvest prospects.¹

The cotton plan has proceeded on very similar lines. The processing tax, however, was to go into operation on August 1st, and, at the time of writing, the amount is not known. The Government hoped to take ten million acres out of production by paying growers \$7 to \$20 per acre (according to the yield of their land) for ploughing under or mowing down cotton already

¹ The harvest prospects may be summarised in the following table taken from the International Institute of Agriculture's *Crop Report and Agricultural Statistics*, July 1933:

Production of Grain in the United States.

Crop	1933	1932	Average 1927-1931	1933 as percentage of	
				1932	1927-1931
Quintals (000's)					
Winter wheat	91,382	125,779	168,885	73	54
Spring wheat	43,522	72,035	69,036	60	63
Rye	6,436	10,124	10,255	64	63
Barley	37,002	65,305	58,981	57	63
Oats	101,451	180,340	171,933	56	59
Maize	508,118	738,673	637,802	69	80

growing¹ The price of cotton also advanced rapidly between March and June, mainly because of a sharp improvement in demand.

At this early stage it is impossible to judge the probable efficacy of the schemes for reducing production and raising prices by transferring to the producer the proceeds of a tax on the consumer representing the disparity between the prices of farm products and those of products purchased by the farmers. There are obvious difficulties in dealing with the prices of the products at later stages of manufacture, with the reactions on consumption and with speculative anticipation of the results expected from the plan. If such "overhead management of agriculture" were to be installed as a permanent system, it would obviously demand extensive planning and regulation of prices and production over a great part of the economic system. It is possible, however, that the experiment is planned only to meet the emergency of the present situation. The Act provides that all stocks of Government cotton shall be liquidated by March 1st, 1936.

It is clear that the agrarian programme as a whole consists of an attempt by Government action on a great scale rapidly to reverse the effects of lowered prices by redistributing income so as to restore agricultural purchasing power. The second phase of the recovery programme attempts this also by giving permissive powers to the President to use at his discretion a variety of inflationary methods to raise prices in general by monetary means. These proposals are contained in the Thomas amendment incorporated in the Agricultural Adjustment Act. The dollar may be devalued to any amount up to 50 per cent; the Federal Reserve Banks may issue a further \$3,000 million of bank-notes secured by Treasury promissory notes; the Treasury also is given power to issue notes, and the President is empowered to accept silver in payment of war debts up to an amount of \$200 million at 50 cents an ounce.

The use that will be made of these powers is not yet known. Coincident with the acceptance of this amendment by the Administration, an embargo was placed (April 20th) on the export of gold, with the result that the external value of the dollar depreciated rapidly. The abrogation of the gold clause in existing contracts referred to in the previous chapter and the refusal of the United States delegation at the Monetary and Economic

¹ Alternatively, the grower may elect to receive cash payments of \$6 to \$12 per acre, together with an option on an amount of Government-owned cotton equalling the reduction in his crop at 6 cents a lb. The scheme was immediately successful in restricting acreage, over 11 million acres being ploughed in or mown down, reducing the estimated acreage from 40.8 to 29.7 million acres. The harvest is therefore expected to fall from 16.6 to 12.3 million bales, as compared with 13 million bales in 1932, 17.1 million in 1931, and 13.9 million in 1930.

Conference to consider plans for currency stabilisation must be considered as part of the same phase of the recovery plan. Prices in general, aided by speculative anticipation of possible inflation, jumped immediately, and production, galvanised by the possibility of increasing costs of production, and by a general expectation of recovery, increased very rapidly before any use was made of the powers conferred under the Act. The diagrams reproduced in the final section of this chapter (see pages 320-1) reveal the extent of the rise in prices produced. Between April 19th and July 26th, the average level of wholesale prices in the United States rose approximately 25 per cent; but in the middle of July, a sharp recession occurred in certain markets. The future course of prices and the use that may be made of the inflationary powers conferred by the Act remain obscure at the moment of writing. It seems clear that the depreciation of the external value of the dollar was a concomitant rather than a cause of the price advance which was due primarily to domestic factors. The falling exchange, however, acts as a barrier against any inrush of imports to take advantage of higher domestic prices.

The rapid rise of prices and expansion of industrial activity in May and June led to the third phase of the recovery programme — an effort by governmental initiative in the regulation of industry to promote employment and raise wages, with the object of increasing consumers' purchasing power so as to keep pace with increasing production. The National Industrial Recovery Act, in which these aspects of the plan are incorporated, consists of two main sections dealing with the regulation of labour and industrial conditions, and a comprehensive programme of public works and unemployment relief. To take the latter section first, a new organisation is created — the "Federal Emergency Administration of Public Works" — to make loans for construction purposes. The Secretary of the Treasury is authorised to borrow for this purpose \$3,300 million. Operations under this part of the Act are expected to terminate within two years, and earlier if the President by proclamation, or the Congress by joint resolution, shall declare the emergency to be ended. In connection with this programme, various other measures (later incorporated in the National Industrial Recovery Act) should be mentioned — the Muscle Shoals power project, adopted on April 10th; the Wagner Direct Relief Act, signed on May 12th, setting aside \$500 million for unemployment relief, 50 per cent of which is to be used in subsidising public works schemes undertaken by States, the remainder being granted to public authorities whose relief funds are exhausted; and the Act creating a Civilian Conservation Corps to give relief work to 250,000 men in the national parks and forests.

The first section of the Act and the spectacular drive to put its provisions into force through the National Industrial Recovery Administration have, however, attracted most public attention. Essentially it is a plan for the regulation of industry by the application of labour codes and competitive conditions, voluntarily agreed and supported by public opinion.¹ Certain industries, notably cotton manufacturing, were able to agree quickly upon codes of labour conditions, wages, hours, etc., which received the approval of the National Industrial Recovery Administration ; but progress in other industries was slow, and on July 24th a "blanket code" applicable to industry in general was approved by the President, to come into force on August 1st. Vigorous propaganda was immediately set on foot to bring all industries within the scope of the plan, either by codes voluntarily agreed upon or under the "blanket code". It is obviously difficult quickly to secure agreement upon labour conditions and competitive codes in widely differing and often unorganised industries, as well as in wholesale trade and retail distribution. The major elements in the plan are provisions for higher wages, shorter hours and recognition of trade unions. The President is given power to license firms and, if need be, to withdraw such licences and thereby prohibit recalcitrant firms from operating. Greatest reliance up to the present, however, has been placed upon the pressure of public opinion and upon the enlistment of voluntary support in a national campaign for recovery. Apart from the stipulation that all firms engaged upon enterprises connected with the public works programme shall conform to the new codes, no Government action, other than persuasion, had been taken up till the end of July to enforce the plan.

In the midst of the first efforts to develop the National Industrial Recovery Administration, before the public works schemes are thoroughly under way, and while the regulation of agrarian production is not yet developed and the future course of monetary policy is not clear, it would obviously be premature to estimate the effects of the experiment.² It is not yet clear

¹ The Emergency Railroad Transportation Act, signed on June 17th, consists of a plan to re-organise the railroad system. A Federal Co-ordinator is appointed to supervise competition, prevent duplication and increase railroad efficiency. This is a notable reversal, in many respects, of the policy pursued by the Interstate Commerce Commission, which was in general opposed to amalgamations.

² The administration of the plan is concentrated in the National Industrial Recovery Council, consisting of members of the Cabinet and the heads of the ten following administrations :

1. National Industrial Recovery Administration — to regulate, direct and approve codes of fair competition for industrial groups.

2. Transportation — to co-ordinate economic adjustments among the railroads, reduce wasteful competition and encourage financial re-organisation.

[Footnote continued on following page.]

whether it will come to be regarded purely as emergency legislation, to be abandoned as soon as conditions improve, or whether part of it will survive and constitute a permanent change in the organisation of the country.

As the following table shows, there has been a marked increase in industrial production.

*Industrial Production in the United States, adjusted for Seasonal Variation.*¹

(Base : Average 1923-1925 = 100.)

Month	Industrial production			Construction		Factory employment	Factory pay-rolls ²	Department stores sales
	General index	Manu- fac- tures	Mining	Total	Resi- dential			
1929 (average).	119	119	115	117	87	101	108	111
1930 (average).	96	95	99	92	50	88	87	102
1931 (average).	81	80	84	63	37	74	66	91
1932 (average).	64	63	71	28	13	62	45	69
1933 : January.	65	64	73	22	8	59	39	60
February	63	61	79	19	8	59	40	60
March .	60	56	81	14	8	57	37	57
April . .	66	66	72	14	10	58	39	67
May . . .	77	77	78	16	11	61	42	67
June . . .	89	90	83	19	14	65	46	66

Continuation of footnote ² on preceding page.]

3. Reconstruction Finance Corporation — to make loans to banks, insurance companies and other financial institutions and to railroads, and in general to finance many of the recovery projects.

4. Federal Home Loan Bank Board — to re-finance mortgages of small home owners by means of a \$2,000 million grant.

5. Federal Emergency Relief Administration — to direct allocation of the \$500 million voted as direct grants to States for unemployment relief.

6. Emergency Public Works Administration — to direct the expenditure of the \$3,300 million voted for public works to provide employment.

7. Tennessee Valley Authority — to develop hydro-electric power at Muscle Shoals and develop the industrial possibilities of the valley thus furnished with power.

8. Civilian Conservation Corps — to employ 250,000 men in reforestation and other conservative projects in national forests.

9. Federal Farm Credit Administration — to direct all farm credit activities, including the \$2,000 million farm mortgage re-financing programme.

10. Agricultural Adjustment Administration — to carry out farm-relief programme, including control of crop production; to direct all marketing activities, including the regulation of grain exchanges; and to levy taxes on the processors of farm products to finance the programme.

(*New York Herald-Tribune*, Paris edition, August 14th, 1933.)

¹ *Federal Reserve Bulletin*.

² Unadjusted for seasonal variation.

It is interesting that, unlike the recovery in the autumn of 1932, recent increases in industrial production have been even more marked in the investment industries than in the consumption industries. This is particularly important in view of the great stress at present being laid upon the expansion of purchasing power and consumption.

*Indexes of Industrial Production in the United States, adjusted for Seasonal Variation.*¹

(Base : Average 1923-1925 = 100.)

Industry	1932		1933	
	July	Maximum reached between August and December	March	June
Iron and steel	25	31	21	72
Textiles	69	104	76	133
Food products	81	95	91	101
Paper, printing	86	91	85	85
Lumber	25	24	22	38
Automobiles	33	60	27	66
Leather and shoes	77	94	85	108
Cement	50	55	40	51
Tobacco, manufactured	114	112	99	135
Coal : Bituminous	46	67	51	63
Anthracite	55	75	77	65

Other information concerning the recovery in the United States is contained in the following section of this chapter.

SYMPTOMS OF RECOVERY.

The greater part of this *Survey* was written in the early months of 1933, before the abandonment of the gold standard by the United States of America and the development of a positive programme of domestic recovery in that country. The material used consisted for the most part of statistical data for the period ending with the first quarter of 1933. Up till that time, the economic situation might be summarised as a drift towards further deterioration after the revival of economic activity in the second half of 1932. Not all of the progress had been lost and there were some favourable developments, such

¹ *Commercial and Financial Chronicle*, July 29th, 1933.

as the improving terms of trade and consequent revival of purchasing power, in certain agricultural countries, notably Australia; but, in face of the failure to break through the tightening restrictions on international trade, the revival seemed to have been checked and in many countries the economic situation threatened to become critical once again.

In the second quarter of 1933, the forces making for recovery appeared to be galvanised into renewed activity by the definite measures taken to raise prices in the United States. By the turn of the year, while the economic situation still retained many ominous aspects and while the great problems of international co-operation remained unsolved, there was no longer any doubt that substantial advances had been made in prices and production. The lowest point of the business cycle appeared to be past. Production had increased, prices were rising, in many countries unemployment was falling and investment was being resumed.

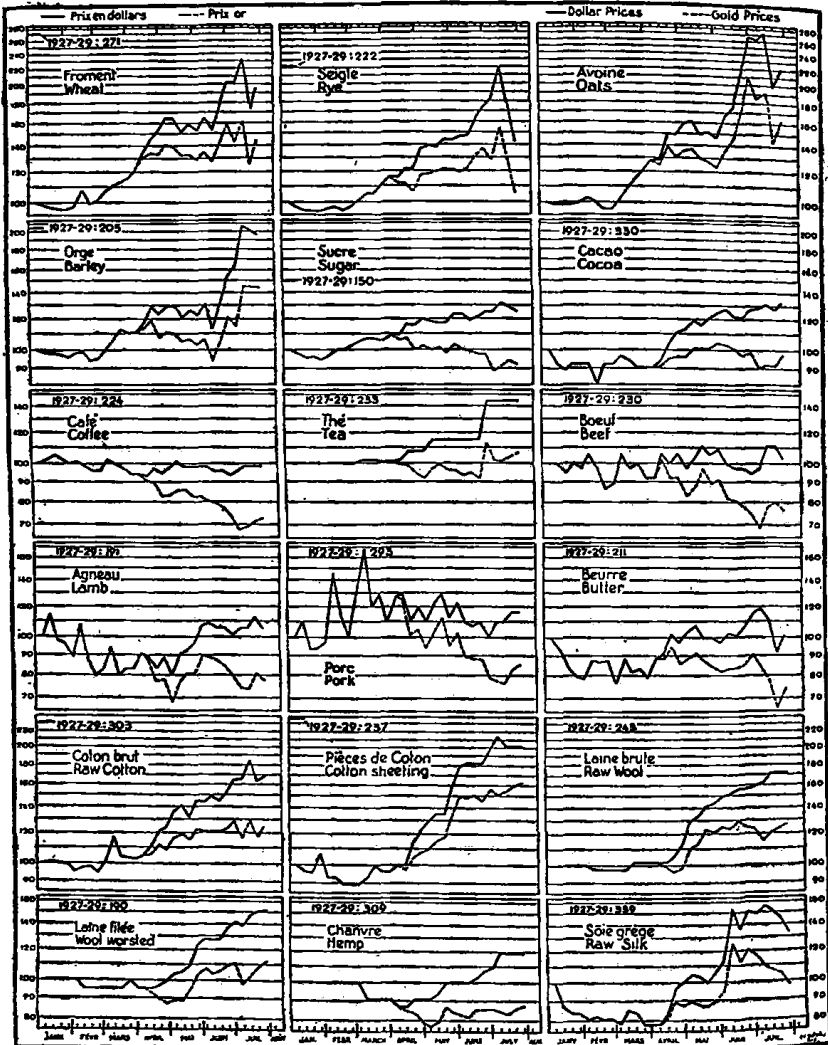
It is interesting to observe the contrast between the developments in the spring of the last three years. In May 1931, the troubles of the Austrian Credit-Anstalt ushered in a period of financial panic. In the spring of 1932 the panic was spent, and the financial improvement betokened by the great conversion operations of the British Treasury, the political settlement which appeared likely after the successful Conference at Lausanne, and the positive monetary action by the Federal Reserve Banks and the Reconstruction Finance Corporation in the United States, together with the natural forces of recovery after a prolonged liquidation of excessive credit, had promoted the first real signs of economic recovery since the depression began. The recovery now in progress in the summer of 1933 is more substantial than that a year ago, and, while it is obvious that many difficulties and obstacles remain which may cause setbacks during the winter months, more confidence has been generated and there has been genuine improvement of price equilibria.

The rise in the price-levels which has occurred has been most marked up to the present in the United States and, as the following diagrams clearly indicate, it is for the most part a rise in paper prices.

In this connection, it should be observed that the rise of prices in the United States between April and July was markedly less than the depreciation in the exchange value of the dollar. In other words, the dollar appeared to be undervalued in terms of other currencies — a phenomenon that occurred also when the sterling exchange first depreciated and in almost every other case of exchange depreciation. Speculation is active in foreign exchange, and fears of further depreciation induce forward

*The Rise of Wholesale Commodity Prices in the United States,
January-July 1933.¹*

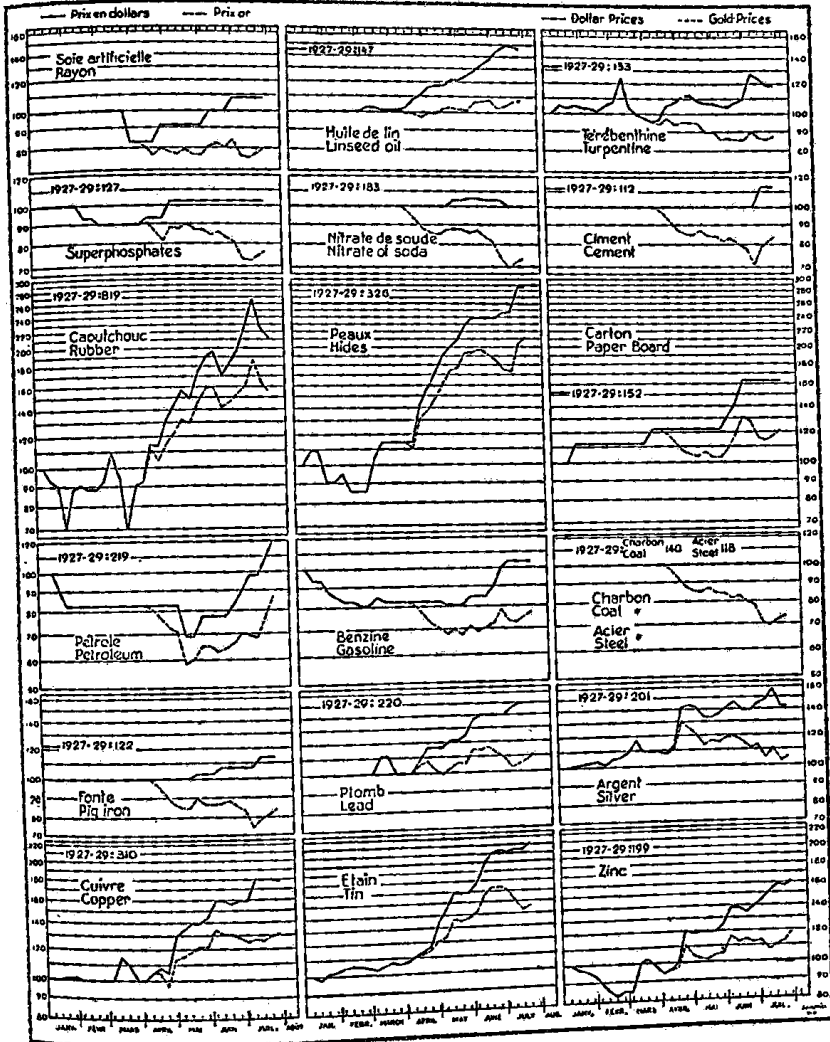
(Base : January 1933 = 100.)



¹ League of Nations *Monthly Bulletin of Statistics*, August 1933.

The Rise of Wholesale Commodity Prices in the United States, January-July 1933 (continued).¹

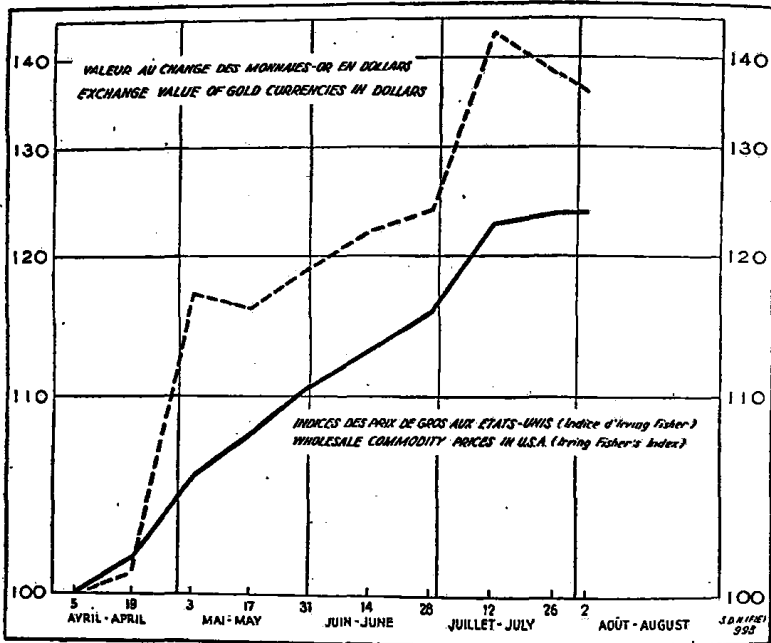
(Base: January 1933 = 100.)



¹ League of Nations *Monthly Bulletin of Statistics*, August 1933.

selling. There appears, therefore, apart from the effect of price movements in other countries, to be a substantial margin by which prices might still rise in the United States before the internal and external values of the dollar are brought into equilibrium. For convenience of calculation, the depreciation is shown on the diagram below in terms of the gold parity; but it should be remembered that sterling and all the currencies associated with it remained stable in terms of the gold currencies during this period.

The Internal and External Value of the Dollar.
(Base : April 5th, 1933 = 100.)



While the rapid increase in dollar prices revealed in these diagrams is greater than the rise either in gold prices or in other national price-levels, there has been, as the following table proves, a widespread, if slower, tendency for the average levels of wholesale prices in many countries to rise.

While the rises in the average price-levels so far recorded have been slight compared with the heavy fall after 1929, they have largely been the result of increases in the prices of those raw materials and foodstuffs which had fallen most heavily.

Index-Numbers of Wholesale Prices.¹
(Base : 1913 = 100.)

Country	1930	1931	1932	1933						
	Average	Average	June	January	February	March	April	May	June	July
Germany	125	111	96	91	91	91	91	92	93	94
Argentina	122	118	119	113	113	112	112	112	113	...
Australia	147	131	128	123	122	122	125	129	...	...
Belgium	108	90	75	75	75	73	72	72	73	73
Canada	135	113	104	100	99	101	102	105	106	110
Denmark	130	114	113	117	124	123	122	123	123	125
U.S.A.	124	105	92	87	86	86	86	90	93	...
France	112	102	86	83	82	79	79	78	82	81
India	116	96	86	88	86	82	84	87	89	91
Dutch East Indies .	134	105	84	78	77	76	74	75	...	...
Italy	411	342	304	296	293	287	282	282	285	283
Japan	137	116	111	140	136	134	133	134	136	138
New Zealand	143	133	129	125	130	129	129	130	130	...
Netherlands	117	97	78	75	74	72	71	72	73	...
United Kingdom . .	119	104	98	100	99	98	97	99	102	102
Sweden	122	111	108	106	106	105	105	106	106	...
Switzerland	126	110	94	91	90	90	91	92	91	92
Czechoslovakia . .	117	107	98	96	96	95	95	96	98	97

The disequilibria upon which stress was laid in Chapter II have therefore been reduced.

There are other indications that the rise in the general level of prices is beginning to correct the disequilibria between different kinds of prices. The levels of retail prices in most countries have either continued to fall or have risen much less than those of wholesale prices. Agricultural prices have increased more than industrial prices in the United States, Canada and Germany. The relation between export and import prices has improved in many agricultural countries — *e.g.*, Denmark, the Dutch East Indies, Australia and New Zealand.

There has also been a marked gain in industrial production, greater than the seasonal average, not only in the United States, but in many other countries.² In the table on page 325, monthly

¹ *Monthly Bulletin of Statistics*, August 1933.

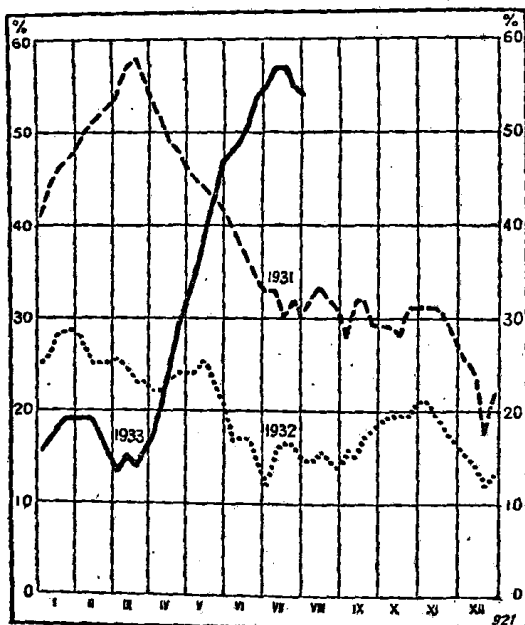
² The index of industrial production in fourteen countries (excluding the U.S.S.R.) published by the Institut für Konjunkturforschung (*Wochenbericht*, August 9th, 1933) was (Base : 1928 = 100) :

	January	February	March	April	May	June
1932	70.8	69.2	68.2	65.3	64.0	63.2
1933	69.0	67.8	66.4	70.5	78.3	85.0

movements of the indices of industrial production are given for the year 1932 and the first six months of 1933.

The evidence of the general indices might be supplemented by more specific indications of improvement in particular industries. In the United States, steel-mill operations, which in the week ending July 5th, 1932, fell to 12 per cent, in the week ending July 1st, 1933, were at 53 per cent, of capacity. Car loadings, electric-power production and similar indices of productive activity also increased very considerably. As the following diagram shows, however, a recession set in about the middle of July. The significance of this recession cannot be appraised at the moment. It may prove to be only a temporary setback in what has been a very rapid advance, or it may possibly indicate serious weaknesses in the present economic position. It is probable, however, that, apart from speculative advances, there was a more solid core of recovery based upon a definite upward swing of the trade cycle.

*Steel Production in the United States.*¹
(Percentage of capacity used.)



¹ *Affärsvärlden*, August 27th, 1933.

*Monthly Indices of Industrial Production, 1932-33.*¹
(Base : 1928 = 100.)

Country	1932												1933					
	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	I	II	III	IV	V	VI
Germany ²	62	63	61	61	62	61	60	59	60	61	62	62	62	64	65	65	68	70
Austria ²	72	75	72	72	63	63	59	62	62	66	66	59	61	61	61	63	64	...
Belgium	72	69	68	67	66	63	49	51	66	69	74	73	72	67	70	70	80	75
Canada ²	68	69	65	58	63	65	63	63	61	60	61	58	53	52	53	55	62	68
U.S.A. ²	65	62	60	57	54	53	52	54	60	60	59	60	59	57	54	60	69	80
France	83	79	77	75	74	73	72	73	74	75	76	77	79	81	83	84	85	88
Japan	96	100	108	104	107	104	107	106	109	113	119	125	117	115	130	126	131	...
Poland ²	52	52	53	55	55	54	54	55	53	56	57	49	47	51	47	53	55	58
United Kingdom ³	90			89			83			90			89			81		
Sweden ²	93	91	96	84	88	77	71	78	82	80	83	84	84	86	86	81	84	82

¹ League of Nations *Monthly Bulletin of Statistics*, No. 8, 1933.

² Adjusted for seasonal variation.

³ The Board of Trade index.

⁴ The production index of the London and Cambridge Economic Service remained constant from the first to the second quarter of 1933. There is normally a definite seasonal decline in the second quarter of the year.

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Changes in the unemployment situation are not so definitely favourable. In Germany, a substantial improvement has occurred in the numbers of unemployed registered (from 6,013,612 in January to 4,856,000 in June). In Australia, the United States and the United Kingdom, the statistics reflect substantial improvement also; but, in practically every other country, unemployment in the middle of 1933 appeared to be greater than in the corresponding months of 1932.

The statistics of international trade up to the middle of the year showed little evidence of improvement. The diagram reproduced as a frontispiece to this volume indicates that the decline in the value of world trade, while slowing down, had not been reversed in the first half of 1932. The most recent statistics available are reproduced in the table below. In the first six months of 1933, world trade fell in value to 34.5 per cent of what it had been in the corresponding period of 1929.

Imports and Exports of Forty-five Countries representing about 90 per cent of the Value of World Trade.
Gold \$ (000,000's).

Year	Imports					
	I	II	III	IV	V	VI
1929	2,836	2,471	2,658	2,872	2,808	2,629
1930	2,605	2,331	2,428	2,321	2,320	2,202
1931	1,743	1,613	1,798	1,715	1,684	1,649
1932	1,141	1,129	1,166	1,151	1,093	1,086
1933	940	898	1,010	.908*	967*	934*

Year	Exports					
	I	II	III	IV	V	VI
1929	2,516	2,299	2,503	2,471	2,414	2,354
1930	2,252	2,072	2,197	2,007	2,068	1,863
1931	1,516	1,445	1,570	1,474	1,450	1,379
1932	994	1,007	1,024	1,004	921	891
1933	848	815	898	773*	834*	837*

Reference has already been made in Chapter X to the almost complete stoppage of foreign lending and to the increasing difficulties in which many countries have been involved in

* Provisional.

meeting their international payments. At the middle of 1933 there had not been time for either the upward movement of prices or the relief given by the depreciation of the dollar to exert a marked effect upon the balances of payments. There is good reason to expect that both these factors will further improve the international economic position of the agricultural-exporting, debtor countries, but the persistence of excessive trade restrictions and other unsolved international economic problems sets obvious limits to any such improvement.

One clear indication of the importance of such unresolved problems is afforded by the harvest statistics for 1933. There has been a considerable failure of the crops in the United States and, to a less extent, in Canada, but the harvest in Europe is abundant. Thus it is estimated that the production of wheat in ten European countries will be 190 million quintals, as compared with 171 in 1932, and it is known that the harvest in other countries, notably France, is large. While the net result in the northern hemisphere will be a substantial diminution in the 1933 crop, the situation is affected also by the possibility of good harvests in Australia, the Argentine and other producing countries in the southern hemisphere.

At the end of July 1933, there was more confidence and greater economic activity in the world as a whole than at any time since the financial panic began in the spring of 1931. The revival in economic activity, however, varied greatly from country to country. The development of the experimental plans for recovery in the United States was being watched with the closest attention, and even anxiety, all over the world. The hope persisted that, whatever the outcome of particular experiments, the forces of recovery evident not only in the United States, but elsewhere, would develop further strength. At the same time, it was clear that great and difficult problems remained unsolved, particularly in the sphere of international economic and financial relations. Indebtedness, currency instability and excessive trade restrictions were obstacles to recovery that could not be expected to vanish without positive action based upon international agreement. Rising prices, increased production and purchasing power, and reviving confidence, leading to more balanced national economic organisation in many important countries, might, it was hoped, make possible in the near future a more positive and constructive approach to these outstanding international problems.

Appendix I.

CHRONOLOGY OF EVENTS, JULY 1932 TO JULY 1933.

1932.

- JULY
- 1 United States of America budget deficit for 1931-32 announced as \$2,885 million.
English Treasury announces conversion of 5% War Loan.
Treasury ban on new capital issues in United Kingdom.
Japan introduces foreign exchange control.
France: General reduction of import quotas (10 to 30 per cent).
 - 5 Beginning of Belgian coal strike (continued to September 7th).
 - 8 Lausanne Agreement signed.
 - 11 Governing Body of the Bank for International Settlements recommends restoration of the gold standard along the lines of the League's gold report.
 - 12 United Kingdom introduces 20 per cent tariffs on Irish goods from July 15th.
Uruguay: Moratorium on commercial debts.
 - 14 Publication of the Belgian, English, French and Italian Gentlemen's Agreement (not to ratify Lausanne Agreement before war debts to United States of America are settled).
 - 16 Ouchy Agreement for tariff reduction initialled by Belgium, Luxemburg and the Netherlands.
 - 18 Turkey becomes Member of the League of Nations.
 - 21 British Imperial Conference opened at Ottawa.
President Hoover signs Emergency Relief and Construction Act, broadening functions of the Reconstruction Finance Corporation.
 - 22 President Hoover signs Home Loan Bank Bill with Glass rider increasing National Bank note issue.
 - 26 Irish retaliatory tariffs imposed on British goods.
 - 28 Bolivia-Paraguay frontier troubles commence.
 - 31 National-Socialists double their number of seats in Reichstag elections.

JULY :

During this month :

Wholesale prices began to rise in the United States, France, India, Japan and the Scandinavian countries. Discount rates were lowered in Danzig, Hungary and India and industrial shares began to rise in practically all countries.

AUGUST

- 2 Issue of French colonial loans amounting to 596 million francs at $4\frac{1}{2}$ per cent.
- 3 United States Treasury announces first issue of National Bank notes under Home Loan Bank Act (Glass rider).
- 11 British loan to Estonia, 1,300,000 krone for four years.
- 13 Persian foreign trade monopoly expanded.
- 14 Swiss banks grant Roumania $2\frac{1}{2}$ years' credit, 50 million francs at $4\frac{1}{2}$ per cent.
- 19 United States of America Commodities Finance Corporation created.
Conclusion of Ottawa Conference. Empire Trade Agreements signed.
- 22 Dutch Treasury bonds issued (75 million florins, 3%).
- 24 Austrian National Council ratifies Lausanne Protocol for the new League of Nations loan.
- 27 Compulsory delivery of foreign exchange in Denmark suspended.
- 30 British Treasury announces new conversions (£13 million, $4\frac{1}{2}$ % War Loan and £140 million $4\frac{1}{2}$ % Treasury bonds).
Italian banks reduce deposit interest rates.
Japan creates fund to regulate foreign exchange rate.
Embargo on British capital issues partially relaxed.

AUGUST : During this month :

Production began to increase in the United States, France, Austria, Hungary, Sweden and Czechoslovakia. Wholesale prices began to rise in the United Kingdom, Australia, Canada, Belgium, Switzerland, Czechoslovakia, but there was a recession in France. Discount rates were reduced in Austria, Chile and Japan.

SEPTEMBER

- 1 President Hindenburg signs Economic Emergency Decree.
- 5 Opening of Stresa Conference on South-East European financial and economic questions.
- 6-14 Enquiry by delegation of Financial Committee of the League into the financial and economic situation of Roumania.

- SEPTEMBER 14 Greece makes an arrangement with its creditors with regard to annual interest service.
- 15 Japan recognises Manchukuo.
- 16 Germany refuses to take further part in the Disarmament Conference until its equality of armament rights is recognised.
- 17 French conversion (85 milliard francs of stocks converted into 4½%, 75 years).
- 21 Reduction of German Bank rate to 2 per cent.
- 22 Italian proposal of an international Convention of a forty-hour week brought before the International Labour Office Governing Body.
- 27 German Emergency Decree to relieve agriculture from its interest burden.
- 28 English liberals (Samuel group) retire from National Government.
- Panama : partial moratorium on external debts.
Hungary : Stock Exchange opened for nineteen stocks.

SEPTEMBER : During this month :

Industrial production began to increase in Germany, Belgium and Japan. World production of pig-iron and steel also began to increase. Wholesale prices began to rise in Greece, Italy and the Netherlands, but there was a recession in Canada and Czechoslovakia. Discount rates were reduced in Germany, Sweden and Czechoslovakia.

- OCTOBER 1 Italian foreign exchange regulations gazetted.
- 3 Lytton Commission report published and presented to the League of Nations.
Iraq becomes Member of the League of Nations.
- 4 Australian Conversion 3½% Loan issued.
- 11 British issue of £150 million 2% Treasury Bonds 1935-1938.
- 13 Bolivia : one year's moratorium for bank and private debt.
Brazil : two months' moratorium for all private debts in Brazilian currency.
- 14 Australia : general increase in tariffs, providing increased preference on British products.
- 15 Yugoslavia : default on two Paris Loans (1906 and 1911).
- 17 The United Kingdom gives notice of its intention to terminate the commercial treaty with Russia.
- 21 New Zealand ratifies the Ottawa Agreement.

- OCTOBER 22-26 Third Balkan conference at Bucharest.
31 Preparatory Commission meets in Geneva to prepare World Economic Conference.

OCTOBER : During this month :

Industrial production began to increase in Poland. Wholesale prices began to fall again in the United States, United Kingdom, Italy, Australia, Belgium and Denmark. Discount rates were reduced in South Africa, Denmark, Spain, Hungary and Poland. Industrial shares began to fall in all countries except Japan.

- NOVEMBER 3 Issue of £300 million 3% British Conversion Loan.
8 Franklin D. Roosevelt elected President of the United States of America.
10 English note asking for war debt postponement.
11 French note asking for war debt postponement.
16 Report of British Unemployment Insurance Commission published.
French Post Office Savings Banks reduce interest rate ($3\frac{1}{4}$ to $2\frac{3}{4}$ per cent).
17 Third Indian Round Table Conference opened in London.
Germany : Von Papen's Government resigns.
23 The United States of America refuses postponement of war debt payments due on December 15th.

NOVEMBER : During this month :

Industrial production began to increase in Canada, but declined in the United States and Czechoslovakia. Wholesale prices began to fall in India and Sweden but rose in Yugoslavia.

- DECEMBER 1 Oslo powers negotiate at The Hague in regard to their position at the Monetary and Economic Conference.
Brazilian Government prohibits new coffee plantations for three years.
Italian Government's consent becomes necessary for all future industrial investments.
2 General von Schleicher becomes Chancellor in Germany.
6 President Hoover's message to Congress includes forecast of budget deficit of \$1,142 million.
11 Five Powers sign an agreement at Geneva recognising Germany's equal right to arm, "when such conditions exist which offer security to all nations".

- DECEMBER 11. Germany resumes her position at the Disarmament Conference.
Third English note on war debts. England offers to pay, but only as a part of final settlement.
Third American note. Payment insisted upon according to the war debt settlement.
- 12 Fourth English war debt note.
Sino-Russian diplomatic relations restored.
Anglo-Persian conflict brought before the Council of the League of Nations.
- 13 Herriot Cabinet resigns.
- 15 The United Kingdom pays £29.5 million sterling (£19.6 million gold) war debt instalment to the United States of America out of Bank of England gold reserve.
Instalments also paid by Italy, Czechoslovakia, Finland, Greece, Latvia, Lithuania, Roumania and Yougoslavia.
France, Poland, Belgium, Estonia and Hungary do not pay.
- 18 Little Entente conference in Belgrade.
- 19 President Hoover suggests to Congress the formation of a commission of both political parties to deal with war debts, disarmament, etc.
- 23 The Netherlands postpones ratification of Ouchy agreement until France, the United Kingdom and Germany have accepted the exception from the most-favoured-nation clause involved in the agreement.
The Netherlands : general increase in tariffs.
- 27 South Africa leaves the gold standard.
- 30 French Parliament ratifies the Lausanne Protocol and the Austrian loan.

DECEMBER : During this month :

Industrial production began to fall again in Germany, Austria, Canada and Poland. Wholesale prices began to fall in Finland, the Netherlands and Norway. The discount rate was lowered in Greece.

1933.

- JANUARY 1 Finland : short-term loan of £1,000,000 contracted in Stockholm.
- 9 Second session of the Preparatory Commission for the Monetary and Economic Conference.

- JANUARY 11 Negotiations for an agreement with the creditors of the Credit-Anstalt concluded.
M. Stalin reports to Central Committee and Central Control Commission of Communist Party on the results of the first Five-year Plan.
A programme for the second Russian Five-year Plan announced.
- 11-25 International Labour Conference at Geneva for the reduction of working hours.
- 16 Control Committee of the States guaranteeing the Austrian loan of 1923 met to discuss the issue of new Austrian international loan.
- 17 Yugoslavia : three years' moratorium negotiated on all payments to foreign holders of Yugoslav bonds.
- 20 Close of Preparatory Commission and publication of Draft Annotated Agenda for the Monetary and Economic Conference.
South African pound reaches parity with sterling.
Invitation from the United States of America for a British delegation to discuss the war debt question.
- 23 Italy : Cabinet decides to create an industrial reconstruction institution :
(1) For the financing of industrial enterprises, and
(2) For industrial demobilisation.
- 24 League Protocol concerning financial collaboration with Roumania signed.
- 25 The United Kingdom accepts the invitation of the United States of America to open debt negotiations at beginning of March, but proposes to postpone discussion of economic problems to the Monetary and Economic Conference.
- 30 Opening of official Standstill Conference at Berlin.
Resignation of German Cabinet.
- 31 Herr Adolf Hitler becomes Chancellor of Germany.
M. Daladier forms new French Cabinet.

JANUARY : During this month :

Industrial production began to increase again in Germany. Discount rates were reduced in Hungary and Italy.

- FEBRUARY 1 British Ambassador opens negotiations with Mr. Roosevelt in regard to war debt conferences.
2 Italy announces willingness to participate in war debt negotiations.

- FEBRUARY
- 2 The United States invitation also issued to Latvia, Lithuania, Finland and Czechoslovakia.
 - 4 International Steel Cartel renewed for five years.
 - 6 Hungary terminates all clearing conventions except that with Austria.
 - 8 Mr. Roosevelt invites forty-eight governors of the States to a conference at Washington in March, in order to examine various relief measures.
 - 9 Mr. de Valera becomes Prime Minister of Irish Free State.
 - 11 Hungary : Standstill Agreement renewed.
 - 14 The Bank for International Settlements share of Reichsbank's credit prolonged for three months. British Imperial Committee on Economic Consultation and Co-operation meets. Union Guardian Trust Co. in Detroit closes down. An eight-day banking holiday declared in State of Michigan.
 - 17 Negotiations concluded for renewal of German Standstill Agreement.
 - 20 New York Federal Reserve Bank agrees for ten days to take over forced sales of bills at one-half per cent to strengthen cash reserves of weak banks.
 - 21 House of Commons approves Austrian Loan Bill. Berlin : negotiations begun for the renewal of the municipal Standstill Agreement, expiring on March 15th.
The United States of America : banks in New York and New Jersey permitted to limit withdrawals of deposits. Governor of Michigan assumes dictatorial banking powers.
 - 22 British and French Ambassadors renew negotiations with Mr. Roosevelt in regard to a future war debt conference.
Following upon Ouchy Convention of June 1932. Belgium, the Netherlands and Luxemburg sign trade and shipping agreement on the basis of the recommendations of the Economic Committee of the League.
 - 23 Following ultimatum to China, Japan advances on Jehol.
Re-organisation of Detroit banks planned. Emergency banking legislation in Indiana and New Hampshire.
 - 25 President Hoover signs Couzens Bill. Emergency banking legislation in Maryland, Missouri, Nebraska, Wisconsin, Iowa, Florida and Oklahoma. Banking holiday in Baltimore.

- FEBRUARY 27 Text of Little Entente pact signed by Yugoslavia, Roumania and Czechoslovakia published.
General moratorium authorised in States of Indiana, Missouri, Arkansas and Wisconsin.
British embargo on exportation of arms to China and Japan.
Withdrawals restricted in Ohio and Indiana.
- 28 Pennsylvania, Delaware and West Virginia restrict withdrawals of bank deposits.

FEBRUARY : During this month :

Wholesale prices began to rise in Denmark and New Zealand. Discount rates were reduced in South Africa and India. Industrial shares began to fall in Japan.

- MARCH
- 1 Banking holiday in Kentucky, Tennessee and Alabama. Withdrawals restricted in Washington, St. Louis, Illinois, Arkansas, Philadelphia and Minnesota.
 - 2 Banking holiday in Oklahoma, Nevada, California, Oregon, Louisiana, Arizona, Texas, Idaho, San Francisco. Stock exchange closed.
New York Bank rate raised from $2\frac{1}{2}$ to $3\frac{1}{2}$ per cent.
 - 3 Banking holiday spreads to five more States, making a total of thirty-seven.
 - 4 Inauguration of President Roosevelt.
Banking holiday in New York and Illinois.
All banking operations suspended.
New York Assay Office refuses to sell gold for Federal Reserve notes.
Dealings in dollars suspended and gold bullion market closed in London.
 - 6 German elections return a majority for the Nazi Government.
The United States of America : President Roosevelt decrees national banking holiday ; prohibits all foreign banking operations ; imposes an embargo on gold and silver exportation ; empowers Treasury to permit certain banks restricted operations, including the issue of Clearing House certificates and authorising the creation of special accounts for new deposits.
 - 7 Secretary of Treasury promulgates new rules for banking activities. Federal Reserve Banks resume normal operations. Banks re-open under restrictions.
 - 9 President Roosevelt lays his crisis proposals before Congress.

- MARCH
- 10 President Roosevelt extends banking holiday for indefinite period and signs Banking Bill to support the emergency Decrees to prevent gold hoarding, to control and re-organise banks, to authorise lending to member banks on new collateral and to provide for issue of Federal Reserve Bank notes against individual and corporate assets as well as Government securities.
 - 11 \$200 million of gold returned to Federal Reserve Banks in three days.
 - 13 Four hundred banks re-open in the twelve Federal Reserve districts. Foreign exchange dealings limited. London resumes dealings in dollars.
 - 14 One thousand banks re-open in districts having Clearing House associations. Banking Bill amendment gives non-member banks access to Federal Reserve Banks.
 - 15 General re-opening of United States banks. Hoarded gold returns : \$300 million in ten days.
New York Stock Market re-opens.
Dollar rate with other gold countries touching export point.
 - 16 British plan presented to Disarmament Conference.
 - 17 New British 2½% Conversion Loan, to be allotted in instalments with Treasury Bills.
 - 18 Announcement of Signor Mussolini's Four-Power Pact proposals.
 - 20 President Roosevelt signs Economy Bill involving \$500 million reductions in expenditure on Veterans' Pensions and Federal salaries.
 - 23 Reichstag passes Enabling Bill giving Herr Hitler dictatorial powers for four years.
 - 27 Japan gives formal notice of her withdrawal from the League of Nations.
Arrest of six British subjects — employees of Metropolitan-Vickers Electrical Co. — in Russia, on charge of sabotage.

MARCH : During this month :

Industrial production began to increase in Japan and Canada. Wholesale prices began to rise again in the United States, Canada and Peru. Discount rates were reduced in Austria, Czechoslovakia and Portugal, but increased in New York. Industrial shares rose in Germany, Sweden and Switzerland.

APRIL

- 3 British fiduciary note issue reverts to the normal statutory amount of £260 million.
- 3-14 Financial Committee of the League of Nations enquiry in Bulgaria.
- 5 Agricultural Conference of Eastern European States at Bucharest.
- 6 President Roosevelt signs two Decrees authorising gold payments for commercial transactions ; forbidding the possession of more than 100 dollars in gold under heavy penalties.
- President Roosevelt addresses official invitations to British Prime Minister and to the French Government to visit the United States to conduct preliminary negotiations concerning Monetary and Economic Conference.
- 7 Reichsbank's decision to repay rediscount credit of \$70 million, granted in June 1931, announced to Bank for International Settlements.
- 8 President Roosevelt invites representatives of Italian and German Governments to take part in preliminary discussions at Washington in preparation for Monetary and Economic Conference. Canada, China, Argentine, Japan, Brazil and Chile also invited.
- 9 Germany : Gleichschaltung — law to bring German States and communes under direct control of the Reich. Text of Roumania's new agricultural debt conversion scheme published.
Substitution by Chinese Government of national silver dollar for the tael.
- 13 Roumania approves ratification of the agreement concerning technical co-operation with the League.
- 14 France : Chamber passes 1933 budget with deficit of 4,177 million francs.
- 19 Danish loan of £1 million to be issued in London: The United Kingdom places embargo on Russian goods.
- 20 The United States of America imposes embargo on gold exports.
Thomas amendment to Farm Bill conferring exceptional powers upon President Roosevelt for the regulation and control of United States currency policy presented to Congress.
- 22 Greece requests renewal of American credit of \$7,500,000.
- 23 Conversations between President Roosevelt and Mr. MacDonald open at Washington.

- APRIL
- 23 Soviet Government imposes boycott on British goods and services during period of British embargo on Russian goods.
 - 24 Anglo-Danish Trade agreement signed.
 - 25 United States : Treasury Issue of $2\frac{7}{8}\%$ \$500 million loan reimbursable in three years.
 - 26 Credit-Anstalt agrément with its foreign creditors signed.
 - 28 New concession to Anglo-Persian Oil Company agreed upon.
 - 29 Meeting of Organising Committee fixes June 12th as date of Monetary and Economic Conference in London.
- Conclusion of French Treasury loan of £30 million from British bankers for a period of six months at an interest rate of $2\frac{1}{2}\%$ per cent.

APRIL : During this month :

Industrial production began to increase in the United States. Wholesale prices began to rise in Australia, Chile, India, Switzerland and Czechoslovakia. Discount rates were reduced in New York and Roumania. Industrial shares began to rise in Belgium, Canada, the United States, France, Japan and Czechoslovakia.

- MAY
- 1 Anglo-Argentine commercial agreement signed.
Text of Anglo-German trade agreement published.
The United States Government abrogates gold clause.
 - 4 Decree of Italian Government authorises increase in Customs duties.
 - 6 League commences financial enquiry into the financial and economic situation of Greece.
 - 8 The United States Government proposes a Customs truce.
 - 9 Turkey floats first *tranche* of the £T12 million internal loan.
In a broadcast speech, President Roosevelt made it clear that the gold clause had been definitely abandoned.
 - 10 Austria suspends payments to the Bank for International Settlements for the service of the League loan.
 - 12 Organising Committee — representing eight Governments — unanimously adopts the proposal for a Customs truce to begin at the opening of the Monetary and Economic Conference.

MAY

- 13 Greek Government defaults on payment of its debt to the United States.
Trade agreement between France and Canada. Canada announces new conversion loan of \$375,000,000.
- 16 House of Commons approves Bill for an increase in Exchange Equalisation Fund to £350,000,000.
Issue of internal State loan for first year of second Five-year Plan in Russia.
President Roosevelt appeals to all Powers represented at Disarmament Conference and the Monetary and Economic Conference to bring about successful conclusion.
- 17 Herr Hitler addresses Reichstag on disarmament.
National Industrial Recovery Bill introduced into United States Congress.
Silver stocks in the United States estimated to be at the highest level ever reached.
- 18 Text of trade agreements between the United Kingdom and Norway and Sweden published.
Germany announces intention of paying her service on "gold loans" in paper currencies.
- 19 Germany accepts British plan "as a basis for future Disarmament Convention".
- 20 Anglo-Norwegian trade agreement signed.
- 23 Anglo-Iceland trade agreement signed.
- 25 Negotiations of armistice between Japan and China.
- 26 Meeting of representatives of Germany's public and private foreign creditors in Berlin, to discuss transfer problem.
- 29 Wheat experts from the United States of America, Canada, Australia and Argentine meet in London to consider limitation of production.

MAY :

During this month :

Wholesale prices began to rise in Germany, Austria, Belgium, United Kingdom and Sweden. Discount rates were reduced in South Africa, Danzig, New York, Norway, but increased in the Netherlands. Industrial shares began to rise in the Netherlands, Poland and the United Kingdom, but fell in Germany.

JUNE

- 1 Adjournment of Disarmament Conference.
- 2 Germany : Law for "regulating agricultural indebtedness" promulgated.
- 7 Four-Power Pact initialled in Rome.

- JUNE**
- 9 Moratorium on German external indebtedness officially announced as from July 1st.
 - 12 Opening of Monetary and Economic Conference in London. Discussion in London between representatives of British, French and American Central Banks and Treasuries with a view to controlling exchanges during the Conference.
London Committee formed to protect interests of English long-term creditors in Germany.
 - 13 The United Kingdom announces payment of 10 million dollars (in silver) in acknowledgment of war debt pending final settlement.
 - 16 President Roosevelt signed National Industry Recovery Act.
The United States Congress adjourns till January next.
Agreement reached between Dr. Schacht and German creditors.
 - 26 Conference at Tokio of representatives of Japan, Manchukuo and Soviet Union to discuss sale of Russian interest in the Chinese Eastern Railway.
 - 27 Dollar-sterling rate falls from 4.20 to 4.29 ½.
 - 28 New York closing rate 4.40 for £ — a fall of 5 per cent in two days.
 - 30 Proposed joint declaration submitted for President Roosevelt's approval calling for monetary stability and re-establishment of gold standard — intended for signature by "gold" and "off gold" countries.

JUNE : During this month :

The rise in wholesale prices became practically worldwide.

- JULY**
- 3 Message from President Roosevelt rejecting immediate exchange stabilisation.
Declaration of adherence to gold standard signed by "gold bloc".
 - 5 Fifty-nine countries now recognise Customs truce.
 - 6 British prisoners released in Russia and embargo on Russian goods removed.
 - 8 Central Banks of six European gold standard countries, in collaboration with the Bank for International Settlements, at Bank of France, draw up Protocol covering measures to be taken should their currencies be threatened.
 - 10 Negotiations for an Anglo-Russian trade agreement resumed by Board of Trade.

JULY

- 11 The United States of America cotton industry presents its code.
Monetary and Economic Conference decides to continue its work in connection with non-controversial subjects.
 - 12 Supplementary agreement concluded between Germany and British Committee of long- and medium-term creditors.
 - 13 New Australian Conversion Loan, interest at 4 per cent and redeemable in 1943-1948. Amount, £17,221,191.
 - 15 France announces decision to repay half British credit three months in advance.
Trade agreement between Latvia and the United Kingdom.
The Netherlands: reduction of discount rate from $4\frac{1}{2}$ to 4 per cent.
Hungary to meet coupons due on August 1st for League Loan of 1924, but unable to transfer full interest service in 1934.
 - 16 Steel industry submits its code to President Roosevelt.
 - 20 New British Loan conversion; $5\frac{1}{2}$ % Gold Bonds of 1932 into Treasury Bonds at $3\frac{1}{2}$ per cent.
 - 21 Meeting in Paris of China Committee of League Council to supervise the technical co-operation of the League with the Government of Nanking.
 - 24 "Blanket code" introduced in the United States of America, to come into effect on August 1st, pending consideration of individual codes already presented.
 - 27 Final plenary meeting of Monetary and Economic Conference.
 - 29 Hungary announced internal loan of 20 million pengö to cover budget deficit.
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