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**ECONOMIC COMMITTEE**

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**OBSERVATIONS  
ON THE PRESENT PROSPECTS  
OF COMMERCIAL POLICY**

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# OBSERVATIONS ON THE PRESENT PROSPECTS OF COMMERCIAL POLICY

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## I. General Observations.

The latter part of 1938 and the current year have been marked by political events which have had a paralysing effect upon confidence in the business world, and the tension to which they have given rise has increased the difficulties of promoting international economic co-operation. International political uncertainty, combined with the high level of armament production, inevitably constitutes a sombre background for any recommendations that the Economic Committee may make at the present time.

The Committee believes, however, that it is possible to make constructive suggestions for the improvement of international economic relations, even at a time when men's minds are constantly preoccupied with thoughts of possible war. There is indeed an unparalleled need for constructive thinking, in order that the lessons of the recent past may be rightly learned and turned to good account. It would be easy, but perhaps fatal, to accept a continuance of the present state of international relations as inevitable and to allow ourselves to drift under the pressure of outside circumstances. It is more difficult, but also more useful, to seek means of promoting some measure of international co-operation now and of preparing the ground for bolder measures in the future.

To some extent, no doubt, economic factors have played their part in producing the present political difficulties. If this is true, this is an additional reason for examining carefully the economic factors involved and for suggesting remedies.

In fact, political and economic difficulties react on one another in such a way as to constitute a vicious circle. It would not be

within the competence of the Committee to express any view as to the possibility of breaking through the circle from the political side. But the Committee feels that efforts to promote international co-operation for economic ends should be pursued concurrently with similar activities in regard to political relations. Nor should a slow rate of progress along one of these two paths necessarily retard advances along the other. It may be easier to promote collaboration in economic than in political matters. At least, the Committee is of the opinion that the attempt should be made, for political agreement might be facilitated if there were an upward trend in international trade.

Moreover, the Committee is encouraged by the certain knowledge that the majority of nations are anxious to develop their trade with others, and to bring about a transition to more stable economic conditions. The Committee feels that it should not merely take note of these facts, but that it should pursue its enquiries and formulate recommendations which, if carried into effect, would, it believes, contribute in some measure to the solution of certain of the problems now facing Governments.

It is to be regretted that, at a time when so many urgent problems are crying for a remedy, most of the best energies and thoughts of mankind are being devoted to problems which, however necessary they may be at the present time, will not in their final result contribute to human welfare. The economic problems facing the world to-day are so numerous, so vast and so complex that redoubled efforts are needed if solutions are to be found for them.

It may well be that the solutions which may be proposed will not in every case be capable of immediate practical application, but when, sooner or later, political confidence is restored, plans must be ready if Governments are to take full advantage of more favourable circumstances.

In addition to the urgent economic problems which would in any case need to be faced by our generation, others have been created by the concentration of resources on the production of armaments. One of these problems is that of the effects of armaments expenditure on standards of living. The immediate effect of such expenditure may in some cases be beneficial in bringing about a wider distribution of purchasing power, but sooner or later, if the present tendency for ever-increasing armaments continues,

the result must inevitably be a fall in the standard of living of the populations concerned. Many Governments are already pre-occupied by this aspect of rearmament and by the consequences likely to arise as the production of armaments impinges more and more on the output of other goods. To these factors must be added the effects on standards of living of policies aiming at rendering a country as self-sufficient as possible in time of war, and, in particular, policies of agricultural protection.

Another problem to which rearmament gives rise is that of the transition from a war economy to a peace-time basis. At some time in the future, it will be necessary to slow down rearmament activity, and the problem will be to effect this without seriously impairing economic activity as a whole. Many difficult problems will have to be faced when a return of political confidence permits the nations which are now arming with such appalling rapidity to revert to the conditions of peace-time production. Modern armaments, even on a moderate scale, require the expenditure of very large resources of labour, material and capital. When so large a proportion of the national income in so many States is being diverted to these unproductive ends, and when so many men are being withdrawn from the normal occupations of a peaceful world, it is unnecessary to enter into any elaborate economic argument for the purpose of showing that a difficult period of transition lies ahead of us at some time in the future. The transition will be made even more difficult than it would otherwise be if Governments, in elaborating their armaments policies, have failed to keep in mind the possibilities of preparing plans for the eventual adaptation to peace conditions. In order that such plans may succeed, they should be prepared on the basis of international collaboration.

The Committee would draw the special attention of the Council to this whole problem of the economic repercussions of armament production, including its influence on the standard of living, and hopes that the next Assembly may charge the Economic and Financial Organisation to make a study of it.

The provision of full employment to their working population is in modern technological conditions a problem common to most countries. The creation of work by the State, while it may be helpful in overcoming the depths of a depression, is only a temporary

palliative and, if pursued without regard to the repercussions on the general economy of the country, will give rise to further maladjustments. The stimulation of internal productive activity creates a need for additional imports, while discouraging the exports necessary to pay for these imports. Hence the balance of trade becomes adverse and exchange difficulties tend to become more and more acute. This is particularly the case when the internal activities are concentrated on armaments and similar non-economic production. In such circumstances, even the richest country will find itself confronted with a shortage of raw-material supplies. This shortage may be relieved, but is not likely to be remedied, by the manufacture of substitutes to replace natural commodities which are available at much cheaper prices. Nor can it be remedied by the maintenance of excessive armaments, and still less by actual aggression. The true remedy is to be found in restoring a better international interchange of products, rectifying the present maladjustment between industrial and agricultural production and restoring a world level of prices based on free exchanges. In a word, it is by means of peaceful economic collaboration that the maximum prosperity can be attained by the people of every country, and it is this economic collaboration which will provide each country with its living space—that is to say, full opportunities for the development of its economic life.

If this principle could be recognised as the basis of national policy for all countries, and confidence in the future solidly restored, it would enable the resources at present expended on unproductive armaments to be applied to improving the standard of life, and a new era of prosperity would open which would raise the well-being of mankind to an unprecedented level. Whether the world is destined to realise this hopeful prospect or, on the other hand, to be torn to pieces in a struggle of which no man can foresee the final end depends on the decisions of Governments.

## II. Recent Trends of International Trade.

The movement of international trade in 1938 and the early months of 1939 has been influenced largely by the trend of business activity in the United States of America, by the expansion of

expenditure on armaments, particularly in Europe, and by considerations related to the probable wartime needs of different countries.

In 1937, the volume of world trade approached the 1929 level, but the decline in American business in the autumn of that year had far-reaching effects in other countries, and the volume of world trade in the second quarter of 1938 fell 12½% below that of the corresponding quarter of 1937. The recovery in industrial production in the United States in the second half of 1938 and the improvement which followed in other countries led to a new expansion of international trade, though not to the level attained in 1937.

The following figures show recent changes in the quantum of world trade. It should be noted that they are not adjusted for seasonal fluctuations, being based on the 1929 quarterly average.

*Quantum of International Trade.*

(1929 quarterly average = 100.)

	1937	1938	1939
First quarter . . . . .	91	87	90
Second quarter . . . . .	98	86	
Third quarter . . . . .	96	88	
Fourth quarter . . . . .	99	94	

The reduced United States requirements of foreign raw materials, combined with other factors, such as the bumper crops of cereals, gave to that country a very large export surplus in 1938, while the trade deficits of the other principal creditor countries, except Sweden, were lower in that year than in 1937. These developments have placed a severe strain on the balances of payments, and consequently on the purchasing power, of the primary-producing debtor countries, which are suffering from lower prices and reduced demand for their exports, in spite of increased industrial activity. Wheat and other cereals have been further affected by bumper crops, and cotton prices are kept low by the pressure of heavy stocks. On the other hand, the prices of several commodities for which there was an increased demand for armament purposes, or for the building-up of emergency reserves, rose in 1938.

As regards the external trade of individual countries, the most notable features in 1938 were the heavy decline in United States imports, the reduction in the trade of Japan with certain countries,

and the fact that Germany was the only highly industrialised country to increase the quantum and the value of her imports,<sup>1</sup> in spite of a decline in her competitive power in export markets.

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In recent months, there has been a tendency in a number of countries to shift the emphasis from the development of the home market towards an expansion of export trade. This has no doubt been largely due to recognition of the limits to which the home market is subject. Moreover, the need for export outlets, particularly in free currency countries, has become increasingly urgent in the case of many countries which desire to replenish their exchange reserves for the purpose of paying both their foreign debts and the increased imports resulting from the production of armaments. In addition, protection of home producers is already at a high level in most countries, and Governments are not able to resort to new protective measures to the same extent as in earlier years as a remedy for economic troubles.

The efforts to secure export markets have tended to accentuate the contrast between the free currency system and the closed currency system of trade. By the free currency system is meant the system under which the proceeds of imports can be freely utilised or withdrawn for purchases in third countries. Under the closed currency system, on the other hand, the exchange accruing to traders is blocked and can only be used for purchases in the importing country.

It would be a mistake to try to apply this classification rigidly to all countries and to all aspects of their economic relations with the rest of the world. There are in fact many shades of economic policy. For example, some of the countries which normally apply the free currency system have felt it necessary to conclude clearing or payments agreements with certain other countries, in order to obtain payment of the claims of their own nationals, and, in these cases and to that extent, their policy approximates to a closed currency system. Moreover, some of the countries which maintain

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<sup>1</sup> Germany's imports (from countries other than Austria) amounted to RM. 5,375 million in 1937 and RM. 5,449 million in 1938.

a free currency nevertheless maintain high tariffs or apply a wide range of quantitative restrictions, thereby restricting the opportunities open to others of obtaining free exchange.

However that may be, the fact remains that certain countries have remained faithful to the principle of a free economy, and have continued generally to practise that system, while others have adopted exclusively the system of a controlled economy.

In the opinion of the Committee, every effort should be made to reduce friction between members of the free currency group on the one hand, and the States with controlled economies on the other.

In this connection, it may be noted that efforts have already been made in certain directions, notably in regard to the international regulation of the coal market. The agreement of principle reached at Düsseldorf between industrialists of the United Kingdom and Germany was another indication that points of contact could be found between the two systems. Though recent events have made it necessary to suspend these and similar efforts, it may be hoped that it will be possible to resume them before long and to bring them to a successful conclusion, on a basis which will favour a rational development of international trade.

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The Economic Committee has already in previous years, and notably in the report which it submitted to the Council in September 1937,<sup>1</sup> put forward suggestions regarding possible measures for securing a relaxation of the impediments to trade, such as exchange control, quotas and unduly high tariffs.

In the following pages, the Committee puts forward a series of interrelated proposals for the consideration of the next Assembly. In formulating them, the Committee has had to bear in mind the limits imposed by present circumstances. But the recommendations contained in the present report, while fragmentary in character and falling short of what would be desirable in more favourable conditions, would be likely, if adopted by Governments, to improve commercial relations in a number of important respects and would, at the same time, pave the way for more extensive action at a

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<sup>1</sup> Document C.358.M.242.1937.II.B.



later stage. They are based on the conviction that, even in a rearming world, progress in the direction of greater freedom and equality of trade is possible.

In previous reports, the Committee has been reluctantly compelled to conclude that it was not possible, in present conditions, to effect any substantial measures of international co-operation by means of multilateral conventions. It has refrained from recommending far-reaching agreements which it knew to be outside the range of immediate practical politics, and has confined itself largely to suggesting improvements in bilateral commercial agreements, since the bilateral method seemed to offer the most effective means of securing an expansion of trade.

In saying this, however, the Committee looks forward to the time when it will be possible to resume co-operation on a wider basis for the purpose of improving economic relations. The Committee feels that only concrete and concerted measures designed to promote international trade, on the most liberal basis possible, will check the present trend towards closed economies. It believes that eventually all Governments will be compelled to collaborate with this object in view. The Committee hopes that, at the next Assembly, Governments will state what they consider to be the best methods of securing such collaboration, and at the same time indicate the contributions they are prepared to make in the common interest.

### **III. Recommendations for Action designed to promote an Expansion of World Trade.**

The Committee believes that the countries which desire to see a progressive, all-round expansion of trade on the basis of the maximum possible freedom and equality should adopt an active and positive policy. This policy would be a dynamic one, the aim of which should be to attract all the principal trading countries, with the object of linking all Governments in the pursuit of a common objective—namely, an improvement in standards of living the world over.

To this end, each country should urgently and seriously examine its position with every other with a view to seeing whether there

are not further tariff or other concessions that it would be prepared to make and anxious to obtain. The countries which have maintained free currencies should continue to conduct their economic relations with the rest of the world on the basis of the maximum possible freedom, while countries practising exchange control should take steps to relax their control as opportunity offers, and they should be assisted in every possible way in these efforts by other countries.

### *Commercial Agreements.*

As regards the general principles on which commercial negotiations should be based, the Committee recognises that commercial agreements or improvements in their mechanism do not suffice to create trade. Agreements can do no more than create conditions suitable for its development. The volume of merchandise passing over national frontiers depends mainly on the general state of economic activity, and this in its turn is conditioned to a very large extent by the political situation. The will to trade and the determination to make the fullest possible use of the advantages of international specialisation must also exist if agreements are to have the desired effect.

It is desirable that agreements should be concluded for a sufficiently long period to enable a certain stability to be given to the mutual trade relations of the signatories. Unless substantial changes occur in the conditions governing trade, the business community should be enabled to base its calculations on a continuance of the existing tariff (or quota) treatment affecting the importation of their goods into other markets. The conclusion of an agreement for a term of years would not, of course, preclude provisions permitting its earlier denunciation in certain defined circumstances. Nor would it prevent either of the contracting Governments from making unilateral reductions of tariffs, enlarging quotas, or taking any other action for improving the conditions governing import trade.

In the second place, the Committee is of the opinion that commercial agreements should provide for mutual tariff and/or quota concessions on the widest possible scale. In particular, the Committee would urge Governments to revise unduly high rates of duty or unduly low quotas, particularly in the case of the

products of those industries the imports of which amount to only a small percentage of domestic production.

The contracting Governments should grant to each other unconditional and unrestricted most-favoured-nation treatment in the matter of tariffs and their application.

Similarly, the countries imposing quotas should fix the amounts of the quotas as liberally as possible; and, in the administration of the quotas, the principle of most-favoured-nation treatment should be applied. A like practice should be followed when quotas are increased.

In the case of Customs tariffs, the application of the most-favoured-nation clause should not be nullified by the introduction of arbitrary tariff specialisation.

The Committee has followed with interest and appreciation the results of the commercial policy pursued by the United States Government since 1934, which is mainly based on the principles advocated in the present report. It is true that, in spite of the successive reductions in duty rates made since 1934, the American tariff still remains at a very high level; and the actual scope of the programme is limited by a provision in the Act of 1934 which stipulated that the existing rate of any duty might not be decreased by more than 50%. Nevertheless, there can be nothing but praise for the activity and pertinacity with which Mr. Cordell Hull has pursued a policy which, in its premises and essential features, is the one most calculated to restore international trade to a healthy state.

The United States Government has negotiated up to date twenty-one agreements with twenty countries<sup>1</sup> under the Act of 1934, the most important having been the Anglo-American Agreement of November last, the conclusion of which the Economic Committee has noted with great satisfaction. This agreement, together with the one concluded simultaneously between the United States and Canada, was particularly significant in that it involved modifications in the system of imperial preferences built up at Ottawa in 1932. It gave concrete evidence of the desire of the countries constituting the British Commonwealth of

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<sup>1</sup> The agreement with Canada was re-negotiated and extended. It should be noted that the rates provided for in the agreement with Nicaragua were suspended in 1938, and that the agreement with Czecho-Slovakia is no longer in effect.

Nations to seek their prosperity in an expansion of world trade as a whole rather than in the grant to each other of exclusive advantages.

The Committee desires to draw the attention of the Assembly to a resolution on the reduction of trade barriers, passed on December 16th last at the eighth International Conference of American States at Lima.

The resolution in question, which is reproduced as an annex to the present report, refers to the adverse effects of excessive barriers to trade and calls upon the American Governments to reduce them to the greatest extent found possible. It recommends the substitution of reasonable tariffs for other forms of restriction, the reduction of import formalities to a minimum, and the negotiation of trade agreements embodying the principle of non-discrimination.

While recognising that, in formulating its resolution, the Conference had particularly in mind the conditions existing on the American continent, which differ in certain respects from those in other parts of the world, the Committee recommends the Assembly to endorse it.

#### *The Relaxation of Quota Restrictions.*

One of the most serious obstacles in the way of the fuller development of trade is the continued existence of quota restrictions. Even among the countries which have retained freedom of exchange, measures of quantitative control for the purpose of limiting imports have often been adopted.

The Committee recognises that a distinction should be drawn between agricultural quotas on the one hand and quotas applied to industrial goods on the other. Quotas on agricultural goods are sometimes intended to effect an orderly regulation of imports throughout the year and to protect the farmer from violent price fluctuations.

Countries which confine their control of trade mainly to tariff rates frequently find that they obtain no reciprocal benefit in return for the most-favoured-nation benefits which they grant to certain other countries using import quotas.

One solution of this difficulty would be the abolition of quantitative restrictions, or the substitution for them, where necessary,

of increased tariffs. In cases where the latter method is adopted, the tariffs should be on as moderate a level as possible.

The Committee recognises that the substitution of moderate tariffs for quotas might give rise to difficulties in countries which use the tariff only or mainly for fiscal purposes and which have never had recourse to negotiable tariffs.

Failing the complete abolition of quotas, there is still much that countries which impose quotas could and should do with a view to liberalising the system. In particular, the list of goods subjected to quotas should be carefully overhauled at regular and brief intervals (say, every six months), with the definite objects of removing from it as many items as possible and of increasing the amount allocated to importers under the quotas which it is thought necessary to retain.

It has also been suggested that, in cases where the complete suppression of particular quotas is difficult, their place might possibly be taken by Customs quotas, under which a specified quantity of a given commodity is allowed to be imported at one tariff rate, while imports in excess of this quantity are dutiable at a higher rate. The competent authorities in countries using quotas might well consider whether this suggestion could be applied to some at least of the goods which are subjected to quantitative restrictions. Customs quotas allow of a reduction of duty and, at the same time, provide domestic producers with protection.

Where quotas must be considered, at least for the time being, as forming part of a country's commercial policy, the most-favoured-nation principle should be applied, as already pointed out above. If discrimination in this respect is practised by countries using quotas, countries using tariffs and prejudiced by such discrimination consider that it would be unfair to expect them to continue to grant most-favoured-nation treatment in regard to tariffs to the offending country.

In this connection, it may be noted that the commercial agreements of the United States contain a clause which states that, in the allocation of the quantity of restricted goods which may be authorised for importation, the other country will be granted a share "equivalent to the proportion of the trade which it enjoyed in a previous representative period prior to the establishment of

such quantitative restrictions". The more widespread application of such a principle in the administration of quotas would do much to attenuate the defects of the quota system.

If quantitative restrictions are considered necessary, they should be rendered as little irksome as possible to the trading community and should be so devised as to reduce to a minimum changes in the direction which trade would take if complete freedom were allowed. The arbitrary diversion of trade into uneconomic channels is not a necessary corollary of quotas.

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The question has been raised whether quotas and also other trade restrictions could be relaxed by free currency countries in regard to other free currency countries while being maintained in full in regard to countries practising exchange control. In support of this suggestion, it was pointed out that the position of free currency countries is radically different from that of countries maintaining exchange control and that the latter countries have, in fact, many possibilities of practising subsidised dumping and discrimination in trade matters for which quotas may be the only effective means of protection. Further, if no action can be taken about relaxation of quotas in regard to countries not practising such devices until it can be applied equally in favour of exchange control countries, relaxation of these restrictions may be postponed indefinitely.

On the other hand, it was urged that many of the countries practising exchange control claim that this measure is forced upon them by their economic condition, and that the alleviation and eventually the abolition of exchange control depends on the relaxation of restrictions enforced by other countries on their exports. Further, account has to be taken of contractual obligations and in particular of the effect of the most-favoured-nation clause. Moreover, the Economic Committee, desiring as it does to see a general development of trade among all the countries in the world, could not wish to suggest the adoption of measures which tended still further to divide the world into two camps.

It would appear to the Committee that if countries practising exchange control apply measures of such a character as to constitute

discrimination or dumping, it is for the countries affected by such measures to decide whether it is necessary for them to withdraw most-favoured-nation privileges from the exchange control countries in question, but, so long as the latter countries are entitled to these privileges, it appears that any relaxation of quotas and similar restrictions should be extended to them, as well as to free currency countries.

The Committee trusts, however, that this application of the most-favoured-nation principle will not be regarded as precluding action, which they consider to be in the interests of all countries, leading to the widest possible relaxation, and eventually the abolition, of quantitative restrictions on international trade.

#### *The Most-favoured-nation Clause.*

It has already been indicated that the Committee in general deprecates derogations from the most-favoured-nation clause. No other system has proved so effective in extending the advantages of bilateral agreements beyond the narrow limits of the direct and immediate interests of the signatory States. For if two countries make a treaty under which they reduce tariffs on certain goods or grant other concessions, these reductions and concessions automatically extend to all countries enjoying most-favoured-nation treatment; and the vast majority of the countries of the world do enjoy such treatment. Furthermore, the effects of the application of the clause are cumulative, for the purchasing power of each country is increased by the growth of its exports resulting from this generalised reduction in tariffs, and as its purchasing power develops, its imports from other countries expand. Though the indirect effects are not capable of measurement, they are none the less of real importance.

Moreover, the clause is the best safeguard which the smaller nations can have in their relations with their economically more powerful neighbours, since in bilateral negotiations the weaker partner usually has the greater interests at stake.

#### *The Problem of Exchange Control.*

This problem was dealt with in the report <sup>1</sup> submitted to the Council in 1938 by a Committee composed of members of the

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<sup>1</sup> Document C.232.M.131.1938.II.A.

Economic and Financial Committees. Moreover, the Joint Committee for the Study of Clearing Agreements, reporting in 1935, expressed the hope that exchange control would be abolished, at any rate as regards commercial transactions, so that national currencies could once more perform their natural function, which is to be exchangeable without any limitation for all other currencies, and through them for goods. Pending such action, the Joint Committee considered that all proposals designed to counteract, directly or indirectly, the grave drawbacks to international commercial relations, resulting from the application of an artificial exchange rate, should be encouraged. These conclusions still hold good at the present time.

The Committee fully appreciates the difficulties which face certain exchange control countries in seeking means to abolish their control in existing circumstances.

As a result of exchange control, however, certain of these countries find themselves in a position under which their general level of prices is so high as very seriously to impede their exports to free currency countries. A high level of prices is not always an inevitable result of exchange control, still less of that degree of control required to check the flight of capital. It is sometimes the result rather of having continued to maintain the price of domestic currency in terms of others at too high a level. There is no necessary relationship between control of currency and the price at which that currency is controlled.

Another factor tending towards a high level of prices in these countries has been the desire to afford to domestic farmers an adequate return for their produce. But this does not necessarily entail the maintenance of a high exchange value for the currency.

Certain of these countries are reluctant to bring their internal prices into line with those ruling on the world market through an adjustment of their currency. They fear that such a course might lead to inflation or to budgetary difficulties, and also to an increase of prices. There has, however, been no single example in recent years of currency devaluation leading to inflation. Devaluation does indeed require the simultaneous adoption of an appropriate budgetary policy. It is also sometimes argued that the beneficial effects of monetary re-alignment on export trade are only temporary. It is true that currency adjustments cannot in any case create a permanent export premium, but they do nevertheless result in the



permanent removal of the arbitrary impediment to exports represented by an overvalued currency.

A further complication arises from the fact that certain of the larger customers of these countries which themselves have controlled markets are able and willing to offer prices in excess of world prices for their products, since by their purchases they obtain, through the machinery of the clearing system, the right to sell in these smaller markets and, in the execution of this right, they may recoup themselves for the high prices paid by demanding compensating prices for their sales.

Obviously, the countries with which this system is operated must decide for themselves whether in the particular circumstances in which they find themselves it is advantageous or not to check their exports to free currency countries and become specialised on the one or two markets which are prepared to pay artificially fixed prices. But under such a system—and in view of their high costs of production, and the limited range of their exports and consequently of their potential customers—such countries are restricted in the choice of their sources of supply. They may be obliged, in order to liquidate clearing debts owed by their customer, to take goods in exchange at unduly high prices and frequently of a class or quality which they would not select under conditions giving them greater liberty of choice. At the same time, the free currency countries suffer from a curtailment of their exports.

In the opinion of the Committee, the exchange control countries should seek every means of so adjusting their position as to make possible the abandonment of control, as soon as circumstances permit.

Since the countries imposing exchange control are in urgent need of foreign currency to meet the service of their debts and to purchase the raw materials required for their industries, it is desirable that, under any clearing or payments agreements which may be negotiated, the free currency countries should leave at the free disposal of the control partner as large a proportion as possible of the exchange derived from their exports. If not rigidly earmarked for specific purposes, the free currency can be used for transactions in third countries, as well as in the country of that currency, thus attenuating the strict bilateralism of full clearings and permitting a step in the direction of a partial restoration of the

multilateral system of trading. The extent to which one free currency country can leave *Devisen* at the disposal of the control countries in this way depends largely on the extent to which other free currency countries pursue a similar policy.

It should be remarked in this connection that clearing agreements themselves have in certain cases been rendered less rigid by a provision which earmarks a percentage of the proceeds of exports from the exchange control country to the specific purpose of purchases of raw materials. The Committee recognises the value of provisions of this kind.

Where circumstances permit, one method of relaxing exchange control which deserves consideration is the system under which the control partner in bilateral agreements allows a part of the foreign currency obtained for its exports to be sold at free market rates, though the general control of exchange may be maintained and the official rate remain unchanged. In this way, it is enabled to sell its goods more easily in the free market and to increase its assets in the currency of the other country. But there is a danger that, if this system is applied to too restricted an extent, the price of the currency may be unduly depressed owing to the narrowness of its market. The extension of this type of agreement over the widest possible area, as suggested above, will help to avert this danger. In some cases where such arrangements are made, it may be necessary to take steps to prevent the market from being disorganised through speculation and a flight of capital from the exchange control country. Speculation of this kind in the currency placed on the free market may lead to a heavy fall in its market value and, apart from other disadvantages, such a result discourages imports into the exchange control country.

The Committee would draw attention to recent agreements of this type which are along the right lines, although they are complicated by different rates for the same currency according to the purposes for which it may be employed. Examples of this kind of agreement are those concluded recently by Roumania with Belgium, the United Kingdom, France and the Netherlands, which enable the Roumanian exporter to sell on the open market, under certain conditions and for certain specific purposes, a proportion, varying in different cases, of the exchange proceeds of his exports. This system permits the exporter to obtain for his exports an

average rate for each transaction considerably higher than the rate at which he sells the proportion reserved to the National Bank of Roumania, while the Bank still secures a certain amount of free exchange at a low rate to cover the needs of the State and the purchase of certain goods, such as raw materials, which are essential to the economy of the country.

Apart from a complete or partial adjustment of the external value of the currency, an exchange control country which wishes to widen its markets may be able to achieve some measure of relief by lowering the prices of its exports in terms of the overvalued currency. For this purpose, certain countries which have not adjusted their exchanges have sought other methods of mitigating the effect of an overvalued currency on their exports. They have adopted systems under which the Government purchases part of the domestic supplies of primary products and sells abroad at ruling market prices, the difference between the latter and internal prices being thus borne by the State. Under a system of this kind, the producer receives remunerative prices, while the Government is able to secure free exchange. But such a policy has serious disadvantages. It is costly, since Government agencies have to be created. Moreover, the loss on export transactions has to be borne by the community, and if, owing to good harvests, there is a large export surplus, the public finances of the country may be jeopardised. In addition, such a system only prolongs the disparity between internal and external price-levels, which has to be remedied before exchange control can be relaxed.

In order to increase the share of their foreign trade conducted with the free currency countries, every effort should be made by the exchange control countries which wish to escape from that system to increase the range and variety of their exports, and in particular vigorous steps should be taken to bring about the necessary improvements in productive efficiency, in sorting, grading and marketing. In the case of certain agricultural commodities, effective competition is limited by defective marketing methods and a failure to pay sufficient attention to the needs of consumers in the free currency countries. Exporters should give a careful study to market conditions and make every effort to adapt their methods to such conditions; and so far as they can, the importing countries should assist them to do so. There can

be no doubt that, if more of their produce were graded and standardised and if buyers were assured of uniform quality and careful packing, sales could be substantially increased. The Committee trusts that special attention will be given to the problem of efficient marketing at the forthcoming Rural Life Conference.

The free currency countries are anxious to promote trade with the exchange control countries, and, especially in recent months, a number of them have shown their readiness to do everything possible for this purpose. But they are not in a position to offer prices in excess of those ruling in the world market, for, obviously, if an importer bought at a higher price in one market than his competitor in another, he would not be able to resell at a profit at home. Purchases above world prices would in fact involve the licensing of imports and the regimentation of trade. Moreover, if such a system were to be effectively applied, it would entail the granting of exclusive favours to a particular group of countries and in this way would constitute a derogation from the most-favoured-nation principle.

The free currency countries should open their markets as widely as possible and, in so far as they are creditor countries, they should be prepared to accept a correspondingly passive merchandise balance in their trade. They should do everything in their power to assist the debtor countries in improving their balances of payments. It is particularly desirable that any quantitative restrictions applied to the products of such countries should be examined with a view to their relaxation and their eventual abolition. No system, however elaborate, can be successful unless the free currency countries are prepared to buy. If both parties look upon trade solely in terms of sales, trade can never flourish, for beneficial trade cannot be one-sided.

In this respect, the creditor countries have a special responsibility, as their resources constitute the reservoirs of purchasing power on the free flow of which world trade largely depends. We recognise that some of these countries have in the past had great difficulties in maintaining their economic position as the result of the efforts to maintain the gold parity of their currencies when other countries had already devalued. But the special measures of protection—especially the widespread application of quotas—which were adopted to defend their currencies and balances of payments have

been maintained, notwithstanding the fact that their currencies have subsequently been readjusted and the special justification for measures of defence for their balance of trade has accordingly disappeared. Some of these countries are now enjoying a revival of economic and financial prosperity, and we would address a special appeal to them to re-examine the need for their restrictions on imports in present conditions. We trust they will take steps, as soon as possible, to relax such restrictions to the fullest possible extent.

Credits are of value as an adjunct to general policy, but they should not be used indiscriminately as a means of forcing exports on to countries which cannot pay for them. In themselves, they can only be regarded as palliatives, since they must eventually be settled out of the proceeds of commodity sales. Moreover, if credits were to be granted on any large scale, they would involve concerted measures among several Governments, and there appears to be little possibility of such action at the present time. On the other hand, there still exist many openings in a number of debtor countries for the investment of capital on an equity basis for the purpose of financing production and organising sales abroad. Such investments can, of course, only take place if there exist reasonable prospects that the service of the loans will be punctually met.

Moreover, manufacturers in the free exchange countries might be encouraged, in suitable cases, to set up branch factories in the smaller exchange control countries. While promoting exports of capital equipment from the creditor country, this system would help to diversify production, relieve the pressure of population on the land and raise living standards in the country where the plant was installed, thus making them less dependent on the export of surpluses of a few staple products.

It may also in certain cases be possible to overcome to some extent the difficulties of trade between the exchange control countries and free currency countries by the formation in the latter of companies to conduct a barter trade, under which the loss incurred by purchases in the control countries could be covered by an equivalent gain from sales to them. Methods of this kind may be a useful expedient in some cases, but in the last resort they can only be regarded as makeshifts.

*Trade between Agricultural Countries and Industrial Countries.*

So far, the Committee has been considering trade primarily from the point of view of the principal restrictions impeding its further expansion. It wishes, however, to make some observations of a general nature regarding the relations between the two principal categories of countries, considered from the standpoint of their economic structure—viz., the predominantly agricultural countries and the predominantly industrial States.

The economic structures of the agricultural countries differ greatly, but they have many features in common. A number of them specialise in the production and export of large quantities of a few agricultural products and, in spite of the recent development of their industrial capacity, they are still largely dependent on these exports for the means to pay for imports and for the service of their external debt. Owing to this dependence on the export of a few commodities, their economic position is highly vulnerable. They cannot readily adopt the device of high internal prices to compensate their producers for low world prices, since the proportion of goods sold on the domestic market is often small. Moreover, no agricultural country can adjust its production to variations in world demand so rapidly as industrial countries are able to do. Thus, in a depression, the terms of trade tend to move violently against the agricultural States,<sup>1</sup> and this fact in turn intensifies the depression.

It is to the interest of the predominantly industrial countries

<sup>1</sup> The terms on which industrial and agricultural (or mining) countries exchange their products are determined by the relationship between the prices of primary products on the one hand, and manufactured articles on the other. The following table, extracted from the *Review of World Trade, 1938*, published by the League of Nations, is of interest in this connection. It gives the movement of the average prices of goods entering into world trade for each main group of articles and shows that the gold prices of foodstuffs and raw materials are still at a lower level compared with 1929 than the gold prices of manufactured articles :

*Price Movement in Gold (1929 = 100).*

	1929	1932	1937	1938
Foodstuffs . . . . .	100	52	45.5	43
Materials, raw or partly manu- factured . . . . .	100	44	47	42.5
Manufactured articles . . . . .	100	63.5	51.5	50.5
All articles . . . . .	100	52.5	48	45.5

to do everything in their power to assist the agricultural States to find remunerative markets for their products. For though the industrial countries may derive temporary benefits from the fall in the price of their imports, they also ultimately suffer through the diminished purchasing power of their agricultural customers.

In this connection, the Committee would refer to the growing influence of sectional interests in recent years and to the increasing readiness of Governments to accept claims for protection in various forms. No doubt this development has been forced upon Governments by the pressure of events. The Committee would, however, urge all Governments to pay more attention to the interests of consumers in their legislation and would emphasise its view that, when protection is granted, it should, so far as possible, be accompanied by an obligation on the part of producers to maintain a high level of efficiency and to reduce costs and prices to a minimum.

In particular, the Committee suggests that reconsideration should be given by Governments to some of the more extreme forms of agricultural protectionism which have arisen in recent years. While the need for a prosperous agriculture in the predominantly industrial countries is fully recognised, it may well be that the desired results can be achieved along lines which are at the same time in the general economic interests of such countries and also, it should be added, more consistent with the nutritional needs of consumers.

The Economic Committee awaits with interest the report of the Delegation on Economic Depressions, which, it understands, may contain some discussion of such questions as the terms of trade of agricultural countries and also problems connected with stocks of raw materials and foodstuffs. The Committee does not propose to make any suggestions in this connection until the report of the Delegation has been issued, but it intends at a later stage to undertake a study of the particular problems of the predominantly agricultural countries and of the relations between them and industrial countries.

#### IV. Conclusion.

Though, in present circumstances, the political situation precludes far-reaching recommendations for application in the immediate

future, it is to be hoped that conditions may soon become propitious for renewing the attempts to bring together the free currency systems on the one hand and the closed currency systems on the other.

Meanwhile, the Committee hopes that some progress may be made along the lines it has suggested. As it has already emphasised, agreements or improvements in their mechanism cannot in themselves create trade. But if the will to trade exists and if Governments are imbued with a determination to foster their economic relations with each other, much can be done to strengthen the links between individual countries.

The enquiries made by the Economic and Financial Organisation of the League into the nutrition problem and the study which is being conducted into measures for raising standards of living have revealed the wide gaps existing in even the most advanced countries between physiological needs on the one hand and actual consumption on the other. There is immense scope for increased consumption, and progress is not impeded by any lack of means for producing and distributing the goods required for raising the general level of material welfare. A great advance in standards of living might have been achieved had the increased technical efficiency of recent years been used to the best advantage.

If the energy and resourcefulness which are now being used to increase military preparedness could be directed towards devising concerted measures of economic and social development and raising the standard of human welfare, no one can foretell the advances that might then be made possible.

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ANNEX

RESOLUTION APPROVED ON DECEMBER 16TH, 1938,  
BY THE EIGHTH INTERNATIONAL CONFERENCE OF  
AMERICAN STATES, AT LIMA, PERU

Considering:

That the full economic development of nations requires the greatest possible volume of mutually profitable international trade;

That such a volume of trade cannot be developed while excessive barriers exist whether in the form of:

(a) Unreasonably high tariffs;

(b) Quotas, licences, exchange controls and other types of quantitative restrictions;

(c) Methods of administering commercial, exchange and monetary policies which impair the maintenance of complete equality of commercial opportunity as between all foreign supplies;

That all such obstacles to trade create unemployment, lower standards of living, limit opportunities for economic advancement, obstruct the fulfilment of broad social programmes, divert trade into uneconomic channels and tend to create international friction and illwill; and

That the American Republics have at previous conferences expressed their support of measures intended to halt further increases in, and to bring about the persistent elimination of, unreasonable and excessive barriers of all kinds to international trade:

The eighth International Conference of American States resolves:

1. To reaffirm the declarations of the seventh Inter-American Conference at Montevideo and Conference for Maintenance of

Peace at Buenos Aires calling upon the American Governments to reduce, to the greatest extent found possible, all existing types of restrictions upon international trade;

2. To endorse the negotiation of trade agreements, embodying the principle of equality of treatment, as the most beneficial and effective method of extending and facilitating international trade;

Recommends:

1. That the Governments of the American Republics substitute, as rapidly as possible, reasonable tariffs *in lieu* of other forms of trade restrictions, inasmuch as experience has shown that such tariffs tend in general to be less restrictive and more susceptible of administration on the basis of most-favoured-nation treatment than are any of the other forms of control over trade and payments;

2. That they reduce, by mutual agreement or otherwise, administrative and technical formalities in connection with the importation of goods to the minimum required for the adequate enforcement of the Customs laws;

3. That they proceed, as vigorously as possible, with the negotiations of trade agreements, embodying the principle of non-discrimination; and

4. That they make every effort, by whatever appropriate means are open to each of them, to encourage other nations to adopt, in the conduct of their commercial policies, the methods and principles recommended above.

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