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the Council and the Members  
of the League.]

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**LEAGUE OF NATIONS**

7

**ANNEX TO THE REPORT ON THE  
WORK OF THE LEAGUE 1936/37, PART II**

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**Note by the Secretary-General**

**on the**

**ECONOMIC SITUATION**

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**Series of League of Nations Publications**

**GENERAL ✓**

**1937. 6.**

## NOTE BY THE SECRETARY-GENERAL ON THE ECONOMIC SITUATION

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Following the precedent set last year,<sup>1</sup> this note draws attention to some of the salient economic developments of 1936 and early 1937. The statistical material upon which it is based is drawn from the publications of the Economic Intelligence Service. A brief reference is made to these publications on pages 121-123 of this year's Report, Part I, and in the relevant Chapter of Part II.<sup>2</sup>

In the report submitted to the Assembly in September 1936, emphasis was laid upon the discrepancy which then existed between the price and cost levels ruling in various countries. Most of the world's currencies had been devalued or depreciated and only a small group still remained attached to gold at the pre-depression parity. Prices remained relatively high within the countries concerned and there was a constant deflationary pressure on their national economies. Moreover, the price and cost discrepancies so created formed an obstacle to the removal or mitigation of trade restrictions.

Very shortly after the report was published, steps were taken to remedy these maladjustments. On September 25th, 1936, it was announced that the Governments of France, the United Kingdom and the United States had come to an agreement by which the former was to devalue the franc and all were to cooperate "so as to avoid as far as possible any disturbance of the basis of international exchange resulting from the proposed readjustment". The franc was thus devalued as part of an

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<sup>1</sup> See document A. 6 (a). 1936 — Annex II.

<sup>2</sup> *World Economic Survey, Sixth Year, 1936/37.*

*Review of World Trade, 1936.*

*Money and Banking, 1936/37* : Vol. I — Monetary Review. Vol. II — Commercial Banks.

*Balances of Payments, 1935.*

*World Production and Prices, 1936/37.*

*Public Finance, 1928/1936.*

*Monthly Bulletin of Statistics.*

*Statistical Year-Book of the League of Nations, 1936/37.*

*International Trade Statistics, 1935.*

international agreement. Its new parity with gold was fixed within fairly wide limits (1 franc = 43 to 49 milligrammes of gold at 0.900), but the exchange rate at which dealings in francs were resumed immediately after devaluation was about 30% below the former parity.

The devaluation of the franc was a signal for other currency readjustments, which were in fact invited by the Tripartite Agreement. Switzerland and Czechoslovakia devalued their currencies to the new French level; the Netherlands suspended the gold standard and allowed the guilder to depreciate by about 20%; the Italian currency was devalued to parity with the dollar and the Latvian to parity with sterling. Greece pegged its currency on sterling with a slight further depreciation, the Union of Soviet Socialist Republics adjusted the rouble peg from 3 to 4.25 French francs, and Brazil pegged the milreis to the U. S. dollar. Germany, Poland and Austria announced their intention not to devalue; but Roumania took the opportunity of legalising the gold premium (38%) which already existed on its currency.

On October 13th, the Secretary of the United States Treasury, in conjunction with the Chancellor of the Exchequer and the French Minister of Finance, announced the provisional establishment of an official gold market between the three countries. The price of gold was maintained by the United States Treasury at the \$35 per fine ounce which had been paid since January 1934. On November 24th, Belgium, Switzerland and the Netherlands joined the original participants in this official gold market.

It will be recalled that, in its reference to these questions, the Economic Committee, reporting to the Council on September 12th, 1936, expressed the opinion that "no currency adjustment can bring about any improvement in the economic situation unless it is accompanied by a relaxation — leading, we should hope, to ultimate abolition — of exceptional import restrictions." Something was achieved in this direction immediately after devaluation — duties were reduced, quotas removed and exceptional import taxes abolished in some of the countries concerned. Much, however, remains to be done before the full benefit of exchange stability can be secured.

There can be no doubt that not only the devaluing countries, but the world as a whole, benefited considerably by the currency

adjustments outlined above. There has been a sharp recovery of production and general economic improvement in practically all the devaluing countries. Only in France were the benefits of devaluation offset by local factors retarding recovery. The delayed recovery in that country has proved a factor of difficulty in making further progress towards international economic co-operation. A prosperous France is essential for the stability of Western Europe.

The devaluations, combined with a rising price-level, have gone far to smooth out the price discrepancies to which attention was drawn last year.

*Gold Wholesale Price-levels, June 1937.\**  
(1929 = 100.)

*Hungary	78	(70)	Belgium	59	(48)	New Zealand	49	(46)
*Germany	77	(76)	*Czechoslovk.	59	(64)	*Chile	45	(36)
Austria	70	(67)	France	59	(60)	Egypt	45	(44)
Albania	63	(62)	Norway	58	(50)	Australia	44 <sup>b</sup>	(41) <sup>b</sup>
*Bulgaria	63	(56)	United Kingdom	58	(50)	British India	44	(39)
*Turkey	63 <sup>c</sup>	(63) <sup>c</sup>	*Roumania	57	(48)	Peru	42	(38)
*Poland	63	(56)	*Latvia	56	(72)	*Japan	37	(31)
*Danzig	62 <sup>b</sup>	(58) <sup>b</sup>	Sweden	56	(48)			
Netherlands	62	(62)	Switzerland	56	(65)			
*Portugal	61	(53)	*Italy	55	(71)			
			*Yugoslavia	55	(50)			
			*Denmark	54	(47)			
			Finland	54	(48)			
			United States	54	(49)			
			*Estonia	52	(47)			
			Union of Sth Africa	52 <sup>d</sup>	(50) <sup>d</sup>			
			Canada	52	(45)			
			*Greece	52	(47)			
			*China	51	(43)			

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- \* Countries applying exchange-control.
  - <sup>a</sup> Index-numbers for corresponding month of 1936 shown in brackets.
  - <sup>b</sup> May.
  - <sup>c</sup> December of the preceding year.
  - <sup>d</sup> July.
  - Calculated on basis of free exchange rate (May).

By comparison with the gold price-levels of June 1936, those for June 1937 show a much closer approximation to international price equilibrium. Too much importance should not

be attached to the absolute figures, which are all based on 1929, a year which cannot be regarded as one of equilibrium. What is important is the movement of the price-levels, and it will be seen that, with few exceptions, this movement has been in the direction of greater equilibrium. The price-levels which were relatively low have moved up the scale and those which were relatively high have in many cases been reduced as a result of devaluation. In the case of the exchange-control countries, it is impossible to estimate the true price-levels for purposes of international trade, as the official rates of exchange in fact apply only to a limited number of transactions. The effective maximum level of gold wholesale prices is probably not higher than the 70% of the 1929 level, which is shown for Austria. A great number of countries — including France, the United Kingdom and the United States — now have price-levels between 54 and 59% of the 1929 level. The agricultural countries outside Europe and those in Europe which have attached their currencies to the pound sterling still have price-levels below the average; but prices have recently been rising in those countries, and also in Chile and Japan.

It may be concluded, therefore, that the devaluations effected in September 1936 have succeeded in their main purpose of bringing about a greater measure of international price equilibrium. This has been possible because the exchange rates have been held stable and, with somewhat freer trade, price movements have worked towards equilibrium.

There has been however, one notable exception to the stability of exchange rates. Owing to political and economic developments in France, it proved impossible to maintain the new parity of the franc that was established in September 1936. In March and April 1937, the French exchange rate moved down to the lower limit fixed by the devaluation and, at the end of June, it became necessary to allow the franc to depreciate still further without fixing a new gold parity. In July, the French Government took energetic steps to remedy the budgetary situation that was the immediate cause of the further depreciation and at the same time measures were taken to cope with the economic difficulties that had arisen.

From a broader point of view, it is evident that the currency adjustments outlined above, combined with the increased demands

for raw materials which were in part due to the acceleration of rearmament programmes, tended to widen the circle of recovery. With few exceptions, practically every country showed a more rapid recovery of industrial production in 1936 than in the previous year. There was also a welcome improvement in international trade. The following summary table gives a good impression of the extent of the recovery in production and trade.

*World Production and World Trade, 1929-1936.*  
(1929 = 100.)

	1932	1935	1936	Percentage increase in 1936 as percentage of 1935
<b>Production of raw materials and foodstuffs :</b>				
(a) Foodstuffs. . . .	100.1	100.3	100.2	—
(b) Raw materials. .	71.4	93.5	105.5	12.8
<b>Industrial production : *</b>				
World . . . . .	69.0	95.4	110.5	15.8
World, excl. U.S.S.R.	63.0	85.2	95.4	12.0
<b>Quantum of world trade .</b>	74.5	82.0	85.5	4.3

\* Mining and manufacturing industries.

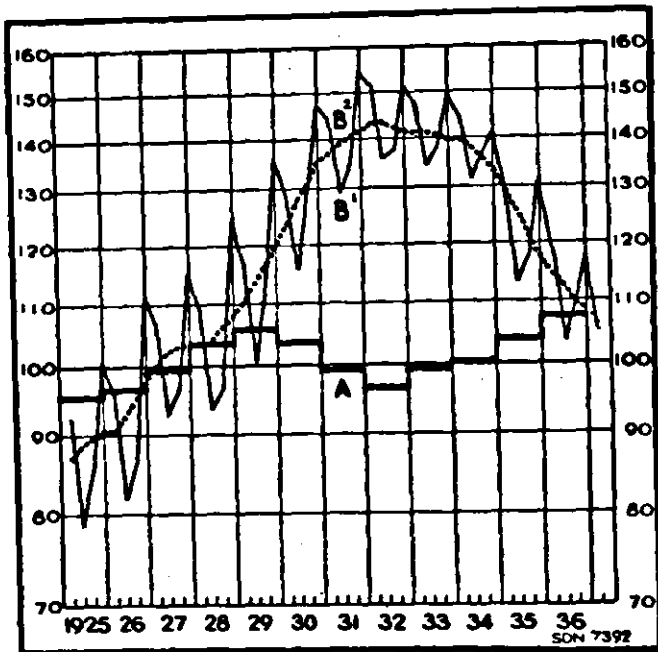
It is quite clear from this table that the increase of industrial production in 1936 was considerable. For the world as a whole, it was greater than in any year since recovery began. Industrial activity increased more than the production of raw materials, partly because raw-material stocks were drawn upon rather heavily, but partly also because of technical progress and to some extent because of the use in certain countries of substitute materials. It is noteworthy also that industrial production increased faster than employment, indicating a continuation of the increase in productivity that has been so marked a feature of the recovery period.

The reduction of stocks of raw materials and certain foodstuffs has been very marked in 1936. For the first time this year, an index, more comprehensive than any hitherto available, has been compiled by the Economic Intelligence Service showing

the extent to which stocks accumulated in the depression period and have since declined. This index is shown in graphical form below.

*World Production and Stocks of Primary Commodities.*  
(Average 1925-1929 = 100 ; logarithmic scale.)

- A Production.
- B<sup>1</sup> Stocks (original index).
- B<sup>2</sup> Stocks (moving average).



In view of the marked acceleration of industrial activity and of the decline in accumulated stocks, it is not surprising that there was a very sharp rise in raw-material prices in the latter part of 1936 and the first quarter of 1937. This rise in prices was enhanced in the case of some commodities by speculative operations which collapsed in the second quarter of the year. It is, however, significant that the falls then recorded left prices of most raw materials considerably higher than they had been a year earlier. In the late summer of 1937, markets were firm and prices were rising again for most commodities.

There was, however, a noticeable difference between raw-material prices and those of foodstuffs. While the prices of certain important foodstuffs, notably wheat, rose considerably in the winter of 1936/37, there were many other food commodities for which prices remained low. The reappearance of the United States and of the Union of Soviet Socialist Republics as wheat

exporters caused a marked relapse in wheat prices also, despite the comparative failure of the Canadian harvest. It is evident that the agricultural producer, despite the boom in agricultural raw materials, faces a potentially dangerous situation as a result of the recovery of production in competitive areas, while former importing markets remain closed.

Nevertheless, the agricultural-exporting countries benefited very materially in 1936 and still more in the first half of 1937 from the rising prices of raw materials and of some foodstuffs. The terms of trade ran in their favour. Their export prices rose, while their import prices lagged behind ; their active export balances increased and they were able in many cases to build up their foreign assets while strengthening their currencies, resuming debt payments on a more adequate scale (even in some cases repaying external debt) and increasing their imports. Not only were price movements in their favour, but there was also an increase in the quantum of their exports as stocks declined and manufacturing demands increased. As their economic situation improved, they were able to increase their imports of manufactured goods, so that, for the first time since the depression, there was general and substantial relief to the export industries of the manufacturing countries.

In consequence of these developments, the value increased more than the quantum of world trade in 1936, but neither increased as much as industrial production. In the last quarter of 1936, industrial activity for the world as a whole was 20.5% above the level of 1929, while the quantum of international trade was still 8% and the sterling value of that trade 31% below 1929.

The recovery of international trade in 1936, however, was more marked than in any previous year since the depression set in. The greater part of the increase was due to the demand for raw materials and this, no doubt, was largely caused by the accelerated rearmament programmes being added to increasing industrial activity in the normal development of the trade cycle. Some part of the increased imports from the raw-material producing countries will doubtless be compensated, after a certain lag, by increased manufactured exports to the raw-material-producing countries ; but there is a danger in the one-way traffic that has resulted from rearmament. There has been a rapid increase



in the passive import balances of all the great industrial countries (except Germany) and it is obvious that this cannot continue indefinitely. Unless there is a substantial expansion of manufactured exports from those countries, there must come a check to the expansion of raw-material imports. It must not be overlooked, however, that many of the raw-material-producing countries are debtors not at the moment maintaining the full service of their external debts, so that their increased exports may be utilised for remedying this situation in the meantime.

The great advance in industrial production in recent months is disclosed in the next table.

*Indices of Industrial Production.*  
(1929 = 100.)

	Average 1932	VI. 1936	VI. 1937
U.S.S.R. . . . .	183.4	368.0	...
Japan . . . . .	97.8	148.0 *	172.7 *
Greece . . . . .	100.9	141.4 *	159.8 *
Sweden . . . . .	90.1	127.0	142.0
Latvia . . . . .	82.4	132.4	139.2
Denmark . . . . .	91.0	133.0	136.0
Hungary . . . . .	76.9	127.4 *	...
Finland . . . . .	83.3	120.0	135.0
Norway . . . . .	92.7	117.7	133.2
Estonia . . . . .	78.3	108.7	131.1
Chile . . . . .	87.0	119.6 *	129.3 *
United Kingdom . .	83.5	115.0	125.5
Germany . . . . .	53.3	108.0	118.1
Canada . . . . .	58.1	88.7	102.5
United States . . .	53.8	86.6	96.6
Belgium . . . . .	69.1	48.5 *	90.3
Austria . . . . .	60.0	78.0	112.0
Czechoslovakia . . .	63.5	75.6	98.7
Poland . . . . .	53.9	71.2	84.2
Netherlands . . . .	62.3	67.9	97.5
France . . . . .	68.8	70.3	73.1

\* April. \* March. • Second quarter. \* May.  
• Labour dispute.

While there still remain wide discrepancies between the degree of industrial recovery in particular countries, they are not quite as marked (except for the failure of production to increase in

France) as they have been. The substantial recovery in the United States is of particular importance, since that country bulks so large in the total of world manufacturing activity.

Comparable statistics of the production of investment as contrasted with consumption goods are lacking for many important countries ; but there is a notable tendency in the great industrial countries for the former — which are already at a high level — to increase more rapidly than the latter. The available statistics are given in the current issue of the *Monthly Bulletin of Statistics*, together with statistics for the production of certain important commodities, such as iron and steel, coal, copper, zinc, textiles, petroleum, automobiles and engineering products.

There is a double explanation for the very marked rise in the production of iron and steel and engineering products in the past year. In part this rise is due to the increase of capital construction that is usual at this stage of the business cycle. In part, however, it is due to rearmament. There is much evidence that the diversion of resources from civil to military production is not only intensifying the boom, but is also beginning to lower the real incomes of consumers. For example, the world-wide shortage of steel has caused delays in production and higher prices, not only for motor-cars, but also for a great variety of other manufactured articles. This is the true cost of rearmament. Standards of living are depressed since real income is lowered. Moreover, concentration upon the heavy industries tends to upset the balance of industrial organisation and to render prosperity more precarious.

In these circumstances, the restoration of world trade takes a new importance. A strong development of manufactured exports from the industrial countries would go far to replace the declining demands of some domestic industries and to forestall the dangers anticipated when rearmament expenditures begin to decline.

During 1936, and still more in the first half of 1937, there was a marked improvement in international trade. In 1936, the quantum of international trade rose by over 5% and its value by nearly 8%. This rate of increase, however, was greatly exceeded in the first half of 1937. The value of world trade in the second quarter of this year was over 31% greater than in the second quarter of 1936, prices having risen sharply and the

quantum having increased by 15 to 96.1%, as compared with 1929 = 100. The greater part of this increase is due to higher export values from certain agricultural-exporting countries. The following summary table shows how greatly exports expanded from some typical countries and how their imports up till the present have lagged behind. It will be seen that these developments are most marked in some South-American and Eastern-European states.

*Exports from and Imports to Certain Agricultural-exporting Countries, 1936/37*

(National currencies.)

Country	Months compared	Percentage Increase in	
		Exports	Imports
Argentina . . . . .	I-VI	95	19
Australia . . . . .	I-V	26	5
Bulgaria . . . . .	I-V	64	37
Canada . . . . .	I-V	21	29
Chile . . . . .	I-V	90	8
China . . . . .	I-VI	45	32
Denmark . . . . .	I-VI	14	25
Egypt . . . . .	I-V	49	11
Estonia . . . . .	I-V	8	31
Finland . . . . .	I-VI	19	47
Hungary . . . . .	I-VI	36	—
India . . . . .	I-V	26	15
Indo-China . . . . .	I-V	49	52
Iran . . . . .	I-V	16	23
Latvia . . . . .	I-V	88	102
British Malaya . . . . .	I-III	48	33
Netherlands Indies . . . . .	I-V	68	68
New Zealand . . . . .	I-VI	23	30
Norway . . . . .	I-V	23	54
Peru . . . . .	I-V	23	2
Portugal . . . . .	I-V	20	14
Roumania . . . . .	I-IV	96	46
Turkey . . . . .	I-IV	56	7
Yugoslavia . . . . .	I-V	80	16

The better economic situation of the agricultural-exporting countries has improved their capacity to meet external debt obligations. There has been an encouraging tendency, not

only for the payments by debtors to increase, but also for creditors to meet debtors halfway by agreeing to interim settlements. Hungary, indeed, has been able to reach a final agreement in respect of the League loan. Much more remains to be done with regard to debt settlements, but the developments in 1936/37 have been encouraging. It is noteworthy that the principal cause of this improvement in the debt situation which has presented so many difficult aspects has been the expansion of international trade.

In the spring of 1937, despite the continuance of favourable economic statistics, there developed a definite check to the upward movement of commodity prices and security values, as a result of which a situation arose which has been described as one of "pessimistic prosperity". In part the fall of prices, which did not in fact go very far, was due to the collapse of speculative positions, and from this point of view the development was not unhealthy. In part, however, it resulted from apprehensions concerning the ability of industry to absorb rising costs of production or pass them on to consumers. Raw-material prices had risen steeply, labour costs of production were increasing, new taxes were being imposed, while freight rates and interest rates were rising also.

At the critical moment, rumours that there might be a fall in the price of gold helped to increase the demoralisation of the security markets. There has not been in fact any reduction in the price of gold, and those responsible for monetary policy in the principal financial countries have steadily denied any intention of making such a reduction. Nevertheless, there has been much popular discussion of an alleged superfluity of gold supplies. The production of new gold from the mines has continued to increase, and there has also been a wave of dishoarding by private individuals and some selling from the reserves of the Union of Soviet Socialist Republics and Japan. The official buying agencies, however, have shown both the will and the power to absorb all the gold offering.

The immediate problem indeed would not seem to be an excess of total supplies, but a maldistribution of gold reserves, and this in turn is due to fundamental economic disequilibria that can only be remedied by a greater degree of freedom in international trade and by allowing changes in trade to be reflected in appropriate price movements. It might have been expected that the improved

trading position of the raw-material-producing countries would lead to a better distribution of gold reserves, and there have been purchases of gold, for instance, from the United States by China and Brazil, together with some signs of renewed hoarding in the Far East. But the first benefits of improved trade were used by the raw-material-producing countries to strengthen their external financial situation, and the rumours that gold was to be cheapened may have made them reluctant to buy it. No one wants to buy a commodity that is likely to fall in price. Fortunately, the gold scare has died down, but a few months ago it contributed a good deal to the unsettlement of the markets and threatened to act as a check to further recovery.

Unfortunately, the problem of controlling prices has been viewed in many quarters mainly as one of credit control or price limitation, or even as necessitating a change in the standard by which prices are measured. The sharp rise, particularly in raw-material prices, in the winter of 1936/37 was clearly leading to a dangerous situation, especially as it was aggravated by speculation. But the obvious means of controlling such an upward tendency is by a reduction of tariffs and other trade barriers. Governments are now in a better position, after some years of recovery and rising prices, to make agreements designed to promote freer international trade and by that means to prevent prices from rising too rapidly. Freer trade is needed, however, not only to control the upward movement of prices at the present time, but also to forestall the dangers that are feared as recovery reaches its crest in the industries that have been most active up till the present, and as rearmament passes its peak.

Some progress has been made in removing obstructions to international trade. There has been a loosening of exchange control, improvement of clearing systems, and a general liberalising of trade restrictions by administrative action. In addition, there have been important developments, such as the reductions of tariffs and abolition of certain quotas that followed the Tripartite Monetary Agreement, the restoration of Italian trade, the signing of a new Franco-German Trade Treaty, the Oslo Agreement and its extension by the application of most-favoured-nation treatment to other countries, and the continuance of the United States' reciprocal trade treaty programme.

Nevertheless, much remains to be done before international

**SOCIETE DES NATIONS**

**ANNEXE AU RAPPORT SUR L'OEUVRE DE LA SOCIETE 1936/37,  
DEUXIEME PARTIE**

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**Note du Secrétaire général**

**sur la**

**SITUATION ECONOMIQUE**

**C o r r i g e n d u m**

Page 5 - Tableau - Lire Chine au lieu de \*Chine.

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**LEAGUE OF NATIONS**

**ANNEX TO THE REPORT ON THE WORK OF THE LEAGUE 1936/37,  
PART II**

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**Note by the Secretary-General**

**on the**

**ECONOMIC SITUATION**

**C o r r i g e n d u m**

Page 5 - Table - For \*China read China.