

COMMERCIAL POLICY
IN THE
POST-WAR WORLD



REPORT OF THE ECONOMIC AND
FINANCIAL COMMITTEES

26410
LEAGUE

ii. A. 7

1945

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LEAGUE OF NATIONS

LEAGUE

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Communicated to the Council
and the Members of the League

Official No.: C.31.M.31.1945.II.A

April, 1945

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LEAGUE OF NATIONS

GENEVA

1945

Series of League of Nations Publications

II. ECONOMIC AND FINANCIAL
1945.II.A.7

Printed in the United States of America
by Princeton University Press, Princeton, N.J.
6/45—3500

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PREFACE

The present report, the preparation of which was decided upon at the 1943 joint session of the Economic and Financial Committees, was completed at a session held at Princeton, New Jersey, in April 1945, at which the following members were present:

Sir Frederick Leith-Ross, G.C.M.G., K.C.B. (United Kingdom),
Chairman

Hon. Robert H. Brand, C.M.G. (United Kingdom)

Mitchell B. Carroll (United States) (Representing the Fiscal Committee)

D. Crena de Iongh (the Netherlands)

W. Domaniewski (Poland) (Replacing J. Nowak)

William A. Fowler (United States) (Replacing the Honorable Henry F. Grady)

F. van Langenhove (Belgium)

F. L. McDougall, C.M.G. (Australia)

Louis Rasminsky (Canada) (Replacing W. C. Clark, C.M.G.)

Winfield W. Riefler (United States)

The following persons, who attended the session in their individual capacities for consultation, participated in the preparation of the report:

Raoul Aglion (France)

Juan Chavez (Peru)

Rafael de la Colina (Mexico)

Josef Hanc (Czechoslovakia)

Kan Lee (China)

J. H. Magowan, C.M.G., O.B.E. (United Kingdom)

Arne Skaug (Norway)

Christian Valensi (France)

The International Labour Office was represented by Mr. E. J. Riches. It was also fortunately possible to arrange for Dr. Richard Schueller, who served as a Member of the Economic Committee for a number of years, to be present at this joint session. The Honorable Henry F. Grady who was prevented from attending has examined the report in its final form and expressed his complete approval of it.

Sir Frederick Leith-Ross and Mr. F. L. McDougall, who attended as members of the Economic Committee, also represented the

United Nations Relief and Rehabilitation Administration and the Interim Commission on Food and Agriculture respectively.

The Committees' report on other matters considered at this session is contained in a separate document.¹

¹ Economic and Financial Committees: *Report to the Council on the Work of the 1945 Joint Session* (Geneva, C.30.M.30.1945.II.A.).

INTRODUCTION

Commercial policy necessarily occupies an important place in the projected pattern of international relationships that is gradually being elaborated by the United Nations on the basis of the Atlantic Charter.

Many of the United Nations have accepted the obligation contained in the Lend-Lease Master Agreement (Article VII) to promote action, "open to participation by all other countries of like mind," directed "to the expansion, by appropriate international and domestic measures, of production, employment and exchange and consumption of goods, which are the material foundations of the liberty and welfare of all peoples; to the elimination of all forms of discriminatory treatment in international commerce, and to the reduction of tariffs and other trade barriers." The United Nations Conference on Food and Agriculture (Hot Springs, May 1943) recommended governments, as part of a programme to bring about a general advance in standards of living, "to reduce barriers of every kind to international trade and to eliminate all forms of discriminatory restriction thereon as effectively and as rapidly as possible." The International Labour Conference (Philadelphia, May 1944), "recognising the great contribution which the international exchange of goods and services can make to higher living standards and to high levels of employment," recommended vigorous action to promote the expansion of international trade. The International Monetary and Financial Conference (Bretton Woods, July 1944), recommended governments to reach agreement as soon as possible on the ways and means whereby they may best "reduce obstacles to international trade and in other ways promote mutually advantageous international commercial relations."

During the greater part of the inter-war period, the Economic Committee of the League of Nations, in conjunction with the Financial Committee, as occasion demanded, was engaged in preparing the ground for inter-governmental action to reduce obstacles to international trade and to secure equitable treatment for the commerce of all nations—aims identical with those which the United Nations are now pledged to pursue. We feel, therefore, that it may be useful for us to offer to governments certain conclusions from our own experience and suggestions on the basis of that experience; and to do so at this stage before the programme of future international action has been drawn up.

The history of international action on commercial policy in the inter-war years constitutes a challenge to the present generation, a

challenge to learn and act upon the lessons of the past, and, above all, to act with determination and in time. If this is done, whatever the difficulties that may be foreseen—and we shall not underestimate them—the prospects for the future will be more hopeful. There exist, moreover, many positive grounds for encouragement. The new emphasis upon full employment and the raising of living standards should go far to alter the whole context in which commercial policies in the inter-war years were formulated. Whereas after the last war little international action to restore economic life was initiated until late in 1920, the United Nations are already attempting to meet some of the more important and urgent problems that will arise at the end of this war. The United Nations Relief and Rehabilitation Administration has been created and is in operation; a Constitution for a Food and Agriculture Organization of the United Nations has been submitted to governments and accepted by twenty-one nations (April 1945); international plans have been devised for the restoration of an international monetary system and to assist in reconstruction and development; the Dumbarton Oaks proposals contain suggestions for setting up a special Council to deal with Economic and Social questions, the need for which has been felt in the past. Much of the technical basis for a more rational framework for international trade has been laid as a result of work carried out by the League and other international bodies; upon this basis, given the will and the conditions necessary for effective action, it should now be possible to build.

Yet much remains to be done to meet the tremendous needs of the future. Wars inevitably change the character and disturb the course of international trade; and the wider the area of war, the more profound are the changes that it causes. After the last war, it was not possible to restore the pre-1914 pattern of trade. The countries which were then the theatre of operations had sustained heavy material damages, were short of industrial stocks and had lost much of their accumulated foreign assets. Their internal finances were in complete disorder and their balance of trade heavily adverse. Currencies collapsed or had to be carefully nursed. The countries which had not been active theatres of operations had developed new industries—often to replace former imports shut off by the war—involving structural changes in the trade of their former suppliers. Throughout the world, production had been stimulated in lines quite unsuitable for peace-time requirements. Debtor and creditor positions had been modified, and in particular, the United States had become the general creditor of the rest of the world. The dimensions of the problems which had to be

solved were never adequately appreciated after 1918 and, though palliatives of various kinds were adopted and eventually a new equilibrium was restored for a time at least, it was the force of the changes caused by the war that shaped economic history.

The present world war has involved hostilities on a far more gigantic scale, has carried destruction to a point of totalitarian intensity and has brought about immense displacements of population. Consequently, its effects on international trade are bound to be still more catastrophic. In many countries economic conditions may well be chaotic for years to come and many measures of restriction and governmental control may be required in order to maintain conditions under which economies can be reconstructed and adapted to peace-time needs. In the attempts to be made to reorganize international trade, account must be taken of this widespread disruption of former trade channels and exceptional measures must be devised to overcome the maladjustments of the immediate post-war period. Otherwise there may be a long period of transition before there will be scope for the development of normal commercial relations.

It is not the purpose of this report to discuss the overwhelming problems of the transitional period, but the Committees feel some doubt whether sufficient attention is being paid to them and fully recognize that unless they are adequately dealt with, the suggestions in this report regarding long-term policy cannot be realized.

CHAPTER I

SUMMARY REVIEW OF OUR WORK, 1920-1939

1. *The Situation at the Time of the Creation of the Economic and Financial Committees*

It was generally believed at the end of the last war that something like the pre-war pattern of international economic relationships could be quickly restored and that no special international action was required for the purpose. By 1920 the bulk of the war-time trade controls had been removed—all too precipitately—outside Europe as well as in the United Kingdom and most of the countries of Northern and Western Europe; but in several of the Continental European countries the partial restoration of relatively free trading was precarious and attempts to effect it had in fact to be abandoned. In Central and Eastern Europe quantitative restrictions were widely retained and such international trade as existed continued to be carried on by means partly of inter-governmental barter, partly by private trading under a system of prohibitions modified by licence. The restricted sector of private trading was further hedged around by currency controls.

The pre-war commercial treaty system had largely broken down after the war; consequently, for many countries, the legal protection against tariff discrimination embodied in the m.f.n. clause had disappeared, while traders were exposed to constant changes both in duties and in the formalities and regulations normally covered by commercial treaties.

More ominous, however, than the actual state of economic relationships were (1) the prevalence of a high protectionist sentiment, not least in the United States; (2) the absence of any international plan, which could be applied immediately after the Armistice, to enable countries to obtain the raw materials and capital goods necessary for the reconstruction of their industries and the resumption of industrial activity.

A partial programme of relief was indeed carried through at an early stage, but the problem of economic reconstruction was not faced as an international issue until the Brussels Conference met in the autumn of 1920. An International Credit Scheme (the ter Meulen Plan) was then unanimously recommended. But exchange depreciation and inflation had gone too far for any international credit scheme to be feasible, so long as the problems of financial reconstruction remained unsolved. Left to themselves, impoverished European coun-

tries felt obliged to prohibit the importation of whatever was not essential and the export of whatever was urgently required at home.

It was in such conditions that the Economic and Financial Committees began their work. It was then too late to devise a general plan for reconstruction. The Governments had worked on the assumption that the world would get back to conditions considered normal prior to the war without any serious difficulty and when this hope was disappointed, the situation in many countries had got beyond control. From 1921 onwards the Financial Committee dealt, and dealt successfully, with the financial problems of a number of countries in Central and Eastern Europe; but the economic problems could not be solved on a purely national basis and international action on the central issues of commercial policy could not be undertaken until financial stability had been restored. Meanwhile, the best contribution to the revival of trade that could be made lay in arranging for the concerted removal of specific restrictions and controls and in improving the legal and administrative basis which governed trading operations. The work of the Economic Committee on these more limited problems met with a considerable measure of success, as will be shown later. At the same time the Committee was able to exercise considerable influence on the development of trade relationships and initiated the negotiation of numerous trade agreements.

2. *Quantitative Restrictions in the 'Twenties*

With the relaxation of political tensions, the passing of conditions of scarcity and the restoration of monetary stability (to which the Financial Committee's work in Austria, Hungary and elsewhere had largely contributed), the way became clear in the middle 'twenties for international action of wider scope.

The most urgent of the central problems calling for such action related to quantitative restrictions. All governments were anxious to see the end of prohibitions and restrictions and in fact endeavoured, as conditions permitted, to reduce their scope by autonomous or bilateral action. There was reason to believe that the remaining restrictions could be eliminated by multilateral agreement.

We were instructed, therefore, to prepare the ground for such an agreement. In the course of this preparatory work, the central difficulty encountered was that of dealing with one form of restriction separately. Quantitative restrictions could be replaced by higher tariffs and it became clear that the prospects of general agreement to

abolish them depended largely upon simultaneous action to reduce excessive tariffs and prevent further tariff increases.

After the meeting of the World Economic Conference of 1927 it seemed likely that this condition would be fulfilled and a Conference for the Abolition of Import and Export Prohibitions and Restrictions was called at the end of the year. An international Convention, based on our draft, was concluded between 30 States, several of which made their signature subject to reservations. In the course of the following year, the scope of these reservations was substantially whittled down and multilateral agreements were concluded and brought into force concerning restrictions on certain products. The general Convention eventually received 21 ratifications as against the 18 necessary to bring it into force. Many of these ratifications, however, were dependent on those of other countries and one "key" country held out because of the retention by another of exceptions which were held to jeopardize its economic life. The negotiations, which had begun with so much promise, finally broke down in the early months of 1930 when, with the spread of the economic depression, the prospects of tariff reduction or even a tariff truce had disappeared.

It thus took about ten years before Continental Europe was ready to complete the process of removing war-time restrictions and then its efforts were frustrated by the sudden collapse in economic activity.

3. M.F.N. and Tariff Levels in the 'Twenties

In Europe, in the early post-war years, tariffs were overshadowed by quantitative restrictions as barriers to trade. But as quantitative restrictions were removed, duties were frequently raised in order to continue the protection which the restrictions had afforded to national industries. Moreover, the new European tariffs introduced in the middle 'twenties were frequently made deliberately high for bargaining purposes; they were not sufficiently reduced by negotiation and tended, instead, to be countered by competitive tariff increases elsewhere. Nor was any considerable progress made with the restoration of the European system of long-term commercial treaties; tariff relationships remained in general unstable and often discriminatory.

The tendency toward higher tariffs was not confined to Europe. Of particular significance was the increase in certain United States tariffs in 1921 and the general tariff increase in that country in 1922.

An international tariff problem of grave proportions thus gradually emerged, and at the World Economic Conference called by the League in May 1927, it was this problem that dominated the discus-

sions. The Conference urged the rapid re-establishment of treaty relationships based upon unconditional and unrestricted m.f.n. treatment, and asserted that "the time has come to put an end to the increase in tariffs and to move in the opposite direction".

The recommendations of the Conference received almost unanimous approval by the Governments of the Members of the League and were endorsed by the League Assembly. They had an immediate, though short-lived, effect. Through autonomous measures or bilateral agreements the upward movement of tariffs was for a time checked. The Franco-German Commercial Treaty of August 1927, concluded under the direct influence of the Conference, laid the basis for an integrated European treaty system, and in the treaties that followed some consolidation of duties was, for a year or more, a notable feature.

It became our main task to facilitate by international action the general adoption of the commercial policy advocated by the Conference. We accordingly set ourselves to:

- (a) codify m.f.n. treatment with a view to facilitating treaty-making along the lines recommended, and
- (b) prepare the ground for tariff reduction by concerted international action, the method upon which the main hopes of achieving effective results had been placed.

(a) *Codification of M.F.N. Treatment*

Our work on m.f.n. treatment may be noted very briefly. We published in 1929 an agreed doctrine concerning the drafting, interpretation and application of the m.f.n. clause.¹ Subsequently we turned our attention to other problems concerning the application of the clause—those, for example, raised by customs quotas and anti-dumping and countervailing duties, the interpretation of the expression "like products" and the question of the nationality of goods.

Had general economic conditions remained favourable, an attempt would have been made to bring about an international agreement on the basis of our drafts. As it was, the drafts were recommended to governments as a basis for administrative practice and commercial treaties. They were widely used by various countries desirous of maintaining a non-discriminatory trading regime. They are annexed to this report for reference (Annex I).

¹ *Recommendations of the Economic Committee Relating to Commercial Policy* (Geneva, doc.C.138.M.53.1929.II.), p. 11.

(b) *Collective Action for the Reduction of Tariffs*

In undertaking to prepare for collective action on tariffs we were breaking entirely fresh ground and realized that in the most favourable circumstances much exploratory work and much laborious negotiation would be required before results could be achieved. We realized, too, that the non-negotiable character of the tariff of the United States at that time, which naturally rendered it difficult for that country to participate in joint action, prejudiced our chances of success.

Two possible methods were first considered: that of "maximum limits", *i.e.*, the fixing by agreement of maximum limits to the duties imposable by any country on each category of merchandise; and that of "percentage reductions", *i.e.*, the maintaining of existing duties in each country as the basis and arranging for simultaneous and gradual percentage reductions in those duties. Each of these methods, however, was considered inequitable by certain countries: the first by those with high tariffs (because others would retain what they would lose, the freedom to raise duties), the second by those whose tariffs were not high (because they felt that they would be penalized in relation to others, especially countries which had inflated their tariffs expressly for bargaining purposes). As with national armaments some years later, so with national tariffs, it proved impossible at that time to find an acceptable general formula on which reductions by different States, with widely varying systems and degrees of protection, might be based.

We then attempted another method. Encouraged by the success of the multilateral agreements for the removal of certain prohibitions, we tried to obtain agreement for the reduction of duties on certain groups of commodities, starting with semi-manufactures, such as cement and aluminium, where there seemed at first to exist a prospect of achieving some results. But it became clear by the end of 1929 that these prospects were not likely to be fulfilled. Less developed countries that were building up their own industries were unwilling to relax protection against lower-cost producers elsewhere, especially in view of the steady rise in agricultural tariffs since 1926. More generally, collective action by groups of commodities raised difficulties of three types: (a) each national tariff being adapted—in theory at least—to the national economic structure, it could be objected that action restricted to one group of products tended to upset the balance of the tariff as a whole; (b) it was difficult to confine action to semi-manufactures since a reduction in the protection afforded to them would

constitute an increase in the protection afforded to the finished goods made from them; and (c) the essence of international trade being the exchange of different kinds of goods, it was far from easy "to find within a single group of commodities that compensatory factor which ultimately underlies every commercial agreement".¹

The preliminary investigations we have just described deserve careful consideration and some of the conclusions to which they lead are analyzed in Chapter II. But it must be emphasized that they were only preliminary investigations at a technical level.

Although trade relations were far from being satisfactory at the end of the 'twenties, considerable progress was being made toward the recovery of international trade, and the volume of world trade was increasing. But how precarious the situation was became clear with the onset of the Great Depression in 1930.

4. *The Impact of the Great Depression*

The decision that inter-governmental negotiations should be attempted was taken by the League Assembly in the autumn of 1929, when the international horizon was already clouded by the deepening agricultural depression and the prospect of a new and still more formidable tariff in the United States. By the time the first diplomatic Conference with a View to Concerted Economic Action opened, early in 1930, the storm had broken. Every government was preparing to defend its national economy against the spread of the depression and desired to maintain its freedom of action. It was no longer possible to discuss tariff stabilization, still less tariff reduction.

In May 1930, the Hawley-Smoot Tariff, the highest in United States history, was finally passed into law. This action, taken at a time when, with the cessation of capital exports, goods should have flowed to the United States in payment of debt and interest, marks perhaps even more directly than the outbreak of the depression itself a turning point in the history of trade relationships in the inter-war years. It was the first major step in the disintegration of trade relationships in the 'thirties and was rapidly followed by a series of further shocks to economic stability, the most serious being the depreciation of sterling and many other currencies in the autumn of 1931. In March 1932, the United Kingdom abandoned its free trade policy and adopted a general tariff; in the following summer a general preferential system was established by the British Commonwealth. Germany

¹ *Report of the Economic Consultative Committee*; Second Session (Geneva, 1929). League of Nations Document C.192.M.73. 1929.II.

and other weak-currency countries which attempted to maintain an artificial parity had recourse to rigorous exchange controls. France made use of import quotas on an extensive scale and developed preferential arrangements within her colonial empire. Throughout a large part of the world, trade was strangled and trade relationships became increasingly discriminatory.

The general negotiations on commercial policy broke down before the end of 1930, and were replaced by a series of limited negotiations aimed at once at developing trade between groups of countries and solving some of the most pressing economic and monetary problems which were driving certain countries ever farther along the road of trade restriction. These efforts and the deterioration of trade relationships referred to above have been traced in League publications¹ and need not be described in further detail here.

The world's hopes of escaping from the *impasse* and of finding a basis on which international trade could be restored, were revived with the calling, at the instance of the Lausanne Reparations Conference, of the London Economic and Monetary Conference in 1933. There was unanimity as to the objectives of economic policy—the same objectives that had been upheld in international gatherings since 1919; but there was no agreement between governments on how those objectives might best be achieved and fundamental difference on crucial issues of immediate policy. More particularly, the United States was unwilling to stabilize the dollar, and the "gold bloc" countries felt unable to bind themselves in regard to trade policy while the future of the dollar was uncertain.

The fate of the London Conference suggests very strongly the unwisdom of convening international diplomatic conferences unless some basic agreement has been reached on the broader issues of policy involved. The breakdown of the negotiations confirmed the trend towards economic nationalism and discouraged further attempts to salvage the world trading system through general multilateral agreement.²

The emphasis in our own work was thenceforth shifted. It was still possible to contribute effectively to the removal of specific causes of trade restriction or discrimination and to assist governments able and anxious to frame policies aimed at restoring a multilateral trad-

¹ See especially *Commercial Policy in the Inter-War Period*, *op. cit.*, pages 52-60.

² The Conference of American States at Montevideo later on in 1933 was an encouraging development, but it did not serve to dispel the general discouragement caused by the failure of the London Conference.

ing system. Some of this work, indeed—for example, the enquiry on Clearing Agreements in 1934-35—had an important influence on certain national policies when recovery got under way. But it was evident that a multilateral trading system could only be restored if there was a real popular demand for it and that that demand would only arise if the average consumer was brought to realize to what an extent his own standard of living was adversely affected by his inability to buy in the cheaper market. The League, therefore, concerned itself more and more with the general problem of how to raise living standards. This approach to the international problem of commercial policy is a heritage of the Great Depression that should not be lost.

5. *The United States Reciprocal Trade Agreements Programme*

The recovery in the middle 'thirties was short-lived and its effect upon economic relationships in Europe limited. In the absence of international measures to overcome the depression, emergency national measures of restriction and discrimination were introduced and in the Axis countries these measures became merged in an over-all strategy of war preparation. In other countries threatened by these developments or within the Axis orbit of influence, economic recovery was built largely upon (a) programmes aimed at achieving the greatest possible degree of national economic independence, and (b) rearmament. Its very basis was thus incompatible with the restoration of a world trading system. But over a large part of the world—more particularly within the sterling area, and between that area and the United States—not only was multilateral trade conserved but progress was made toward freer trading.

At the lowest ebb of international economic co-operation, there occurred a fundamental change in United States tariff policy—the passing of the Reciprocal Trade Agreements Act of 1934. Under this Act, renewed in 1937, in 1940, and again in 1943, agreements based on the unconditional m.f.n. clause have been concluded with twenty-eight countries. Duties on two-thirds of the dutiable imports of the United States (1939 figures) have been reduced, and on 68%, by value, of the items affected, the reduction has amounted to the full 50% permitted by the Act. The reciprocal concessions obtained from the other parties to these agreements, and generalized under the m.f.n. clause, have had the effect, in addition to tariff reductions, of abating discriminatory practices and of modifying preferential systems. A demonstration has been given of what can be accomplished

to counteract restrictive tendencies elsewhere, if one of the world's great consuming countries takes the lead.¹

It is encouraging that a bill has been introduced in the United States House of Representatives to extend the American trade-agreements programme for three years from June 12th, 1945, and to authorize 50 % reductions of customs duties in effect on January 1st of this year.

6. Improving the Legal, Fiscal and Administrative Bases of Trade

So far we have been considering phases of our experience in connection with the central issues of commercial policy from which useful lessons may be drawn. But there is, we believe, much to be learnt also from our experience with more limited problems, or problems on the periphery of commercial policy, on which, by and large, substantial positive results were achieved. Part of this work is embodied in the following multilateral agreements:

¹ The following table from *Commerce Reports*, February 17th, 1940, shows the result of the reciprocal trade agreements programme of the United States up to 1939.

UNITED STATES TRADE WITH TRADE-AGREEMENT COUNTRIES AND WITH ALL OTHER COUNTRIES, 1939 COMPARED WITH 1938, AND 1938-39 COMPARED WITH 1934-35

(Values in millions of dollars)

ITEMS	Comparison of 1939 with 1938				Comparison of 1938-39 with 1934-35			
	1938 value	1939 value	Change Value	Per- cent	1934- 35 average value	1938- 39 average value	Change Value	Per- cent
EXPORTS, INCLUDING REEXPORTS								
Total, trade-agreement countries	\$1,758	\$1,901	+ 142	+ 8.1	\$757	\$1,232	+ 475	+62.8
Total, nonagreement countries	1,336	1,277	- 59	- 4.5	\$992	\$1,306	+ 314	+31.7
Total, all countries	3,094	3,177	+ 83	+ 2.7	2,208	3,136	+ 928	+42.0
GENERAL IMPORTS								
Total, trade-agreement countries	\$1,155	\$1,387	+ 233	+20.1	\$774	\$942	+ 168	+21.6
Total, nonagreement countries	806	931	+ 125	+15.6	\$772	\$868	+ 97	+12.5
Total, all countries	1,960	2,318	+ 358	+18.3	1,851	2,139	+ 288	+15.6

¹ Including the 18 countries (and colonies) with which agreements were in operation during the greater part of the last 12 months. Only 1 of the agreements was in operation throughout 1935, 6 throughout 1936, 14 by the end of 1936, 16 by the end of 1937, 17 by the end of 1938, and 18 by the end of 1939, including the agreement with the United Kingdom (covering also Newfoundland and the non-self-governing British colonies). The agreement concluded with Turkey became provisionally effective only on May 5, 1939, and the agreement with Venezuela only on Dec. 16, 1939. Statistics for these countries are therefore not included in the above calculations.

² These figures do not include Ecuador, the United Kingdom, Newfoundland, and non-self-governing British colonies, Turkey, and Venezuela with which agreements have been concluded but where the period during which the agreement has been in effect is too short to justify inclusion for purposes of comparison.

³ The apparent discrepancy shown by these figures in comparison with the other totals is due to the noninclusion of trade with Ecuador and the United Kingdom and its Crown colonies.

	Entered into force	Number of Parties to Agreement
International Convention relating to the Simplification of Customs Formalities. Geneva, 1923	1924	31
Protocol on Arbitration Clauses. Geneva, 1923	1924	28
International Convention on the Execution of Foreign Arbitral Awards. Geneva, 1927	1929	21
Revised International Convention for the Protection of Industrial Property. The Hague, 1925	1928	31
Six international Conventions for the Unification of Laws relating to Bills of Exchange, Promissory Notes and Cheques: Convention for the Settlement of certain Conflicts of Laws in connection with Bills of Exchange and Promissory Notes. Geneva, 1930	1934	18
Convention for the Settlement of certain Conflicts of Laws in connection with Cheques. Geneva, 1931	1934	17
Convention providing a Uniform Law for Bills of Exchange and Promissory Notes. Geneva, 1930	1934	18
Convention providing a Uniform Law for Cheques. Geneva, 1931	1934	17
Convention on the Stamp Laws in connection with Bills of Exchange and Promissory Notes. Geneva, 1930	1934	20
Convention on the Stamp Laws in connection with Cheques. Geneva, 1931	1933	20
Three international Conventions concerning Veterinary Police Regulations: Convention for the Campaign against Contagious Diseases of Animals. Geneva, 1935	1938	8
Convention concerning the Export and Import of certain Animal Products. Geneva, 1935	1938	6
Convention concerning the Transit of Animals, Meat and other Products of Animal Origin. Geneva, 1935	1938	6

On the removal of double-taxation—a matter of great importance for foreign investment and consequently for the development of trade—model treaties drawn up in 1928 and revised in 1935 and again in 1944, have provided a basis for more than 100 important bilateral agreements.

On the Treatment of Foreigners and Foreign Enterprises a body of principles was worked out between 1923 and 1929. While an attempt to secure general adoption of these principles by international convention failed, they have been used within certain groups of countries in bilateral and regional establishment arrangements.

A Standard Customs Nomenclature, so devised as to be adaptable to the needs of any country, was worked out between 1927 and 1931 and revised in the light of experience in 1937. In spite of the fact that the work was completed so shortly before the war, the Nomenclature has already been adopted in whole or in part by more than a dozen countries.

Rules drawn up in 1937 with a view to removing the principal obstacles to the supply of raw materials, were accepted by a number of governments, including the United States and the principal colonial powers, as a basis for possible international action when circumstances permitted.

Some of the practical lessons from this body of experience, of which only the main aspects have been mentioned, are discussed in the next chapter.

CHAPTER II

SOME LESSONS FROM EXPERIENCE

The main conclusions that may be drawn from the experience of the inter-war period are of two distinct types: (1) those relating to the practicability of carrying through the sort of policies that governments collectively advocated; and (2) those relating to the machinery and procedure for international action. We shall briefly discuss each of these in turn.

1. *Main Factors Impeding Adoption of Liberal Commercial Policies*

The growth of protectionism in Europe after the last war was due to a number of factors, certain of which are likely to present themselves again and, unless popular sentiment can be educated, may prove difficult to eradicate. Others no less threatening may, we believe, be overcome more easily if the lessons of the past are learnt and constructive policies are boldly conceived and executed.

(a) *Political and Economic Insecurity*

Within the first class the most important was undoubtedly the widespread sense of political insecurity. This feeling of insecurity immediately after the last war was a natural heritage of the war itself. It was intensified by the impact on each nation of the rampant nationalism of others—likewise a natural effect of the fighting that had taken place. It was particularly acute in certain countries which had had their frontiers profoundly modified or which had been newly created. These new or greatly changed political entities, which had still to constitute the most elementary machinery of government and communal existence, were naturally and inevitably anxious and hesitant. They were anxious about their own political future; they were hesitant to embark on the high seas of a world trading system. Their instinct was to keep themselves shut off to the greatest possible extent from external forces until they had acquired greater internal cohesion. But even countries which did not undergo territorial changes or were not belligerents learned from experience how deep are the economic consequences of war. The feeling of economic insecurity thus became world-wide and influenced economic, and more particularly commercial, policies everywhere.

There is today a general hope that after the present war effective measures will be taken to assure political security for a long period.

But owing to the destruction wrought by this war, economic anxiety and hesitancy are likely to be widespread and in every country the Government will be pressed to provide employment and social security for its people on the basis of national action without much regard for international reactions. The development of a favourable public opinion in regard to international action will be of the greatest importance and we believe that it will largely depend on the rapidity and effectiveness of the measures adopted to safeguard peace and to revive economic activity.

(b) *The Lack of a Reconstruction Programme*

The second most important cause of the difficulty of reviving international trade after the last war—perhaps indeed it was the most important—was the failure of governments to agree upon and to implement any reconstruction programme. Countries were left, as they will be again, with the most urgent need for every type of consumers' goods and with a desperate lack of raw materials, of machine parts, of railway rolling stock, etc. Almost nothing was done for two years to meet these needs. Inevitably every country sought to keep the little it had—to check export; to acquire by whatever means it could what it required from abroad, and in so doing to sacrifice its credit and to sell its currency for what it was worth. We need not attempt to repaint the picture again here. But the failure to secure agreement on any international plan for recovery was one of the decisive reasons why "commercial policy was driven from the very outset down the wrong road and never found another".¹

But why were the effects of these early failures decisive? Why, when national incomes had been restored to or above their pre-war level in the later 'twenties, were European Governments still hesitant to bind themselves by long-term treaties and anxious to limit the benefit of tariff concessions to those countries that made reciprocal concessions? Why, even after the 1927 Conference, were tariff levels raised rather than lowered?

The failure to devise any collective plan for tiding over the transition period was decisive because, behind every form of protective measures to which governments were driven to defend their markets and exchanges grew up a number of vested interests which resisted—and resisted successfully, in the main—any endeavour to reduce the barriers sheltering them. As a result, the distortion of national econ-

¹ League of Nations: *Europe's Overseas Needs, 1919-1920, and How They were Met* (Series of League of Nations Publications, 1943.II.A.6.).

omies produced by the war were never fully corrected, while serious fresh maladjustments developed and were reflected in over-capacity and unemployment in the older industrial countries and agricultural over-production in the predominantly agricultural countries. The first became haunted by the spectre of unemployment, the second by the spectre of a collapse in export prices; both were reluctant to tie their hands by long-term tariff treaties; both consequently tended to seek greater stability by means of diversifying production, the first by supporting high-cost agriculture, the second by stimulating uneconomic industrialization programmes.

(c) *Inadequate Regard for Consumers' Interests*

The result of these circumstances was that in both industrial and agricultural countries there was a large measure of popular support behind the intensification of trade restrictions. This popular support was in the circumstances natural, as the benefits to sectional groups were obvious and the consequent impoverishment of the general community more difficult to discern. Viewed from another angle, it was the outcome of the two other general causes we wish to underline, first the absence of the voice of the consumer in the determination of policy, and secondly the failure to devise and carry out any general policy for maintaining a high level of employment.

Because the consumer was so largely inarticulate, he was to a great extent politically ignored. In the 'thirties, as we have already mentioned, under the pressure of conditions which shocked the conscience of the world, there was a shift in policy and governments began to think less in terms of production only and more in terms of consumption—of raising living standards. Gradually this new policy gained support and today it constitutes one of the most encouraging factors in political trends. For, once it comes to be recognized that the purpose of production is not simply to provide wages or profits but to render vitally needed goods available to all classes of the population, then the need for removing obstructions between the producer and the consumer becomes patent; then the popular demand for the provision of goods at the lowest possible price is likely to become a weighty influence in the determination of policy.

Unfortunately the movement in favour of improving living standards developed too late to have any great influence on commercial policy before the outbreak of war. But it was growing constantly in strength and has continued to grow during the war years.

(d) *Unemployment and Economic Instability*

In spite of the factors we have been discussing, there was a gradual return towards a stable pattern of trade relationships in the 'twenties and the general increase in tariffs was temporarily checked after 1927. The evidence clearly suggests that the movement would have been continued and that some demobilization of tariffs might actually have been achieved but for the economic depression, the drying up of the flow of international capital and the United States tariff of 1930. For all its uncertainty, the brief period of expansion in the middle 'thirties, following the depression, again brought some improvement in trade relationships.

After the onset of the depression, each government, faced by contracting markets and growing unemployment, endeavoured to secure the home market to its own producers by shutting out foreign goods and used every available means to stimulate exports. Trade warfare was the inevitable consequence. The inescapable conclusion from this experience is that the maintenance of a world trading system depends upon the formulation and successful execution of policies for maintaining a high level of employment, policies which to be successful must be internationally co-ordinated.

If we consider the future in the light of past experience, four essential economic desiderata present themselves :

- (i) the need for adequate and concerted measures to correct the dislocations caused by the war and to enable economic activity to be revived generally;
- (ii) the need to maintain high and stable levels of employment;
- (iii) the need for securing higher living standards;
- (iv) the need for a great expansion of multilateral trade as one of the most important means of providing both employment and higher living standards.

These four needs are interlocked and policies must be formulated which take account of all of them. The importance of securing the adoption of such policies is, we believe, generally recognized today. Adequate plans, national and international, for economic reconstruction along sound lines¹ should lay the foundation for an expanding world economy; the determination of governments to maintain high

¹ See the proposals put forward by the Delegation on Economic Depressions in *The Transition from War to Peace Economy* (League of Nations, Geneva, doc. C.6. M.6.1943.II.A.) and *Economic Stability in the Post-War World* (League of Nations, Geneva, doc.C.I.M.1.1945.II.A.).

levels of economic activity and employment should assure minimum living standards, above pre-war levels, and create an atmosphere favourable to the reduction of trade barriers and the elimination of trade discriminations; a great expansion of multilateral trade should increase employment, increase the productivity of labour and capital and make possible progressively higher standards of living.

2. *Procedure and Machinery*

(a) *Machinery for International Action*

Most of the administrative questions and the questions concerning the legal and fiscal bases of trade which were successfully dealt with had been a cause of concern to governments and the business communities before 1914. Several of them had been the subject of international conferences, but on none had any substantial results been obtained. The progress achieved in the 'twenties, under conditions of intensified economic nationalism and acute economic dislocation, is a clear demonstration of the value of a permanent international machinery: (a) for joint discussion, study and negotiation between responsible national officials; (b) to supervise the execution of multilateral agreements (a function of considerable importance in view of the flexible character of many of the agreements concluded) and to further the gradual assimilation of national practices to standards suggested; (c) to mobilize the co-operation of—and to co-operate with—private international bodies working in the field of commercial policy.

But for dealing with the central issues of commercial policy, the machinery and equipment for international action was inadequate. The powers of the Economic Committee were limited. The headquarters staff at Geneva concerned with questions of commercial policy never exceeded half a dozen senior officials; there was therefore no question of its being able to study in detail the problems and policies of individual countries or to keep in constant touch, as was required, with national administrations throughout the world. The absence was felt, moreover, of any international body with power to mediate or arbitrate, when so requested, in connection with trade disputes between States.

(b) *Value and Advantages of Multilateral Conventions*

Study and negotiation to find the basis for international agreement normally culminated, in the 'twenties, in the calling of a diplo-

matic conference and the signature of a multilateral convention. This procedure has proved to possess many advantages :

(i) it often enables some desired result to be achieved very rapidly—for example, the simplification of customs formalities, which would take many years to achieve by bilateral negotiations ;

(ii) there are things which no country or pair of countries would feel able to do unless they were done simultaneously by many others ;

(iii) it is the only practicable method of creating international legislation of general application ;

(iv) a system set up by a multilateral treaty has a greater stability than can be achieved even by a whole network of bilateral treaties ;

(v) whereas in a bilateral negotiation there must be an approximate balance between the concessions given and received by each contracting party, in a multilateral agreement it is not necessary that concessions between any two countries should be even approximately equivalent so long as each party's concessions are offset by the concessions which it obtains from all the other parties combined.

The advantages of the multilateral procedure were conspicuous in the case of many of the non-tariff problems which we considered, in particular those which raised no serious issues of national interest. The procedure also justified itself—although the results were, in the event, limited—in the case of the attack upon quantitative restrictions in the 'twenties, when such restrictions were considered "artificial" and there was a universal desire to be rid of them. In the matter of tariff reduction, the experience of multilateral negotiation, though inconclusive, was not encouraging and would suggest that a possible alternative form of multilateral action, if general agreement is not immediately practicable, might be the setting in motion of a series of bi- or tri- or limited pluri-lateral negotiations under some central co-ordination, as the first stage before their submission for more general adoption. On this more will be said in Chapter VII.

(c) *Difficulties sometimes raised by the General Multilateral Procedure*

In the early days of the League it was considered necessary to open conferences on such general questions as commercial policy to all States. In certain cases this procedure was found to raise a number of specific difficulties :

(i) national differences in law and practice, as well as in economic conditions, are sometimes so great that agreement is possible only between a few States ;

(ii) when universal agreement is aimed at, there is a tendency to whittle down the obligations imposed and this may result in a code that falls short of the existing practice in the more advanced States; moreover, the weakening of the obligations to secure the signature of doubtful countries may be to no purpose, since these countries may fail to ratify;

(iii) there is inevitable uncertainty whether signature of a multi-lateral convention laboriously prepared and negotiated will be followed by the minimum of ratifications (or the specific ratifications) necessary to bring it into force.

(d) *Methods of Meeting these Difficulties*

In later years attempts were made with some success to meet these difficulties:

(i) *Limited Conventions*: Useful results were sometimes achieved by limiting negotiations to countries particularly interested in some specific problem. The Stresa Convention of 1932 and the Wheat and Sugar Agreements of 1933 and 1937 respectively were cases in point.

(ii) *Model Conventions for bilateral adoption*: Conventions were framed which were intended not to be signed and ratified as multi-lateral agreements but to be used by governments as models for bilateral agreements. The most substantial results have been achieved by this method in connection with the work of the Fiscal Committee on the removal of double taxation. It may be useful to quote the considered opinion of that Committee after several years of experience in the matter:¹

“This procedure has the dual merit that, on the one hand, insofar as the model constitutes the basis of bilateral agreements, it creates automatically a uniformity of practice and legislation, while, on the other hand, inasmuch as it may be modified in any bilateral agreement reached, it is sufficiently elastic to be adapted to the different conditions obtaining in different countries or pairs of countries.”

As mentioned in Chapter I, over one hundred important double-taxation agreements have been concluded on the basis of these League models.

(iii) *Models for autonomous adoption*: On certain matters not lending themselves to formal international agreement, useful results could often be achieved merely by drawing up international stand-

¹ Fiscal Committee: *Report to the Council on the Fifth Session of the Committee, 1935* (Geneva, doc.C.252.M.124.1935.II.A.).

ards either for adoption as and when changes in national legislation or practice could conveniently be undertaken or to serve as a guide for the formulation of policy.

It is to be hoped that the changed conditions caused by the war—while they present many new problems—may also afford a more favourable opportunity for a multilateral approach to commercial agreements on a broader scale.

(e) *Desirability of Broadening the Bases of International Negotiations*

For reasons of convenience, it has in the past been the almost universal practice to limit international negotiations to a single group of problems. While unlikely to impede successful action on questions lying outside commercial policy proper and not directly involving national interests, this limitation may be a serious obstacle to progress on more central issues. We have shown in Chapter I to what an extent the multilateral negotiations on prohibitions and restrictions were affected by the development of the tariff negotiations and *vice versa*.

This point of procedure deserves to be carefully borne in mind in the future and we would suggest that, where the central issues of policy are concerned, no opportunity should be overlooked for either broadening the bases of a single negotiation or arranging for simultaneous and linked negotiations on particular issues, so as to secure a better balance in the prospective benefits to the parties concerned. Clearly, too, the more closely international trade negotiations can be linked with measures for ensuring high and stable levels of employment, the better their chances of success.

CHAPTER III

TRADE AND TRADE POLICY IN THE POST-WAR ECONOMY

We have already noted that one of the major reasons why the removal of restrictions on trade after the last war proved so difficult was the lack of any generally agreed policy of reconstruction, the lack of any financial machinery which would afford to countries short of raw materials, foodstuffs, etc., the necessary breathing space in which to restart production and to adapt their economies to the new conditions that gradually revealed themselves. After this war, the first concern of many governments will again be the provision of those goods from overseas essential for reviving their economic activity, and the gradual adaptation of their whole economy from war to peace needs, from partial or almost total isolation to a world economy. These problems of reconstruction and adaptation have been dealt with in the report of another League Committee;¹ we need not discuss them therefore here. But we must face the fact that this necessary process of adaptation will take time; that we cannot expect the world to move suddenly from the restrictions of a war economy to that measure of freedom which it is the declared purpose of the United Nations to attain.

How rapidly the transition can be effected and how fully those aims can be realized will largely depend, as we have already suggested, on the extent to which statesmen and the general public act on the realization that there is a close interdependence between greater freedom of trade and the achievement of high and stable employment of resources.

1. Commercial Policy and Standards of Living

It is useless to advocate greater freedom of trade for the sake of trade itself or to pursue a commercial policy for the sake of commerce alone. Commercial policy is an integral part of the expansionist policies so widely and so justly advocated today; it is an essential part of all policies to maintain active and efficient employment; it is an essential part of those social policies whose purpose we epitomize in the expression "a high standard of living".

The fundamental reason why greater freedom of trade is necessary for securing a higher standard of living is obvious, for only by inter-

¹ *The Transition from War to Peace Economy.*

national trade is the individual consumer able to purchase what is produced in the cheapest markets, only by this means can he convert his own work into the maximum possible amount of goods and services, the product of the work of others.¹

2. *Commercial Policy and Full Employment*

But the consumer would gain little were he to find that greater freedom of trade implied for him a reduced opportunity for employment. It is only the work he actually performs that he can convert into the goods and services he wants. The League's Delegation on Economic Depressions has just completed a comprehensive report² on the whole problem of maintaining a high and stable level of employment and of avoiding depressions and the misery they entail. Unlike so many other reports on the subject, this document emphasizes the essentially international character of depressions and their spread from country to country through a sudden contraction of trade or of foreign investment. It insists, too, on the inevitable dependence of many classes of countries and of the success of their employment policies on the level and freedom of trade.

"We draw attention", the Delegation remarks, "to the dependence of many agricultural and mining countries upon foreign trade; but certain highly industrialized countries are scarcely less dependent. When capital goods constitute a large proportion of their exports, these industrial countries are particularly susceptible to fluctuations in economic activity abroad. When in addition their imports consist largely of indispensable foodstuffs, their balance of payments becomes particularly vulnerable. Neither these countries nor certain of the smaller industrialized states with highly specialized export industries can hope to maintain a high and stable level of employment by means of domestic compensatory policies alone. It is therefore of vital importance to them, and indeed to the whole world, if standards of living are to be upheld or improved, that the volume of world trade should be maintained and that sudden changes in either the direction or the composition of that trade should be avoided. More than a mechanism to permit the smooth transfer of international payments is required. If depression and the spread of depression from market to market are

¹ The effects upon living standards of the high agricultural tariffs that developed in many industrial countries in the inter-war years was brought out in the final report of the League of Nations Mixed Committee on Nutrition: *The Relation of Nutrition to Health, Agriculture and Economic Policy* (Geneva, doc.A.13.1937. II.A.), pp. 206-226.

² *Economic Stability in the Post-War World.*

to be obviated, there is need both for the will to maintain a high level of economic activity and income and for the will to maintain a multi-lateral system of trade in which all are able to participate under conditions at once equitable and stable.”¹

The crucial importance of foreign investment and foreign trade, especially in crude materials, is further insisted upon by the Delegation. “These critical factors are neither accidents nor special manifestations of an individualistic organization of society; underlying them are the elemental facts that raw materials and agricultural resources are not evenly scattered over the globe in proportion to population and that many peoples do not have a sufficient margin between their production and their minimum consumption needs to provide solely out of internal saving for the development which they need.”² They terminate this section of their report with the following conclusions:

“The ability of most countries to achieve sufficient control of their internal situation to permit the successful application of the most appropriate contra-cyclical policies, in fact, requires international understanding and in some cases international action of five distinct forms. . . . They are:

- “(1) the adoption of more liberal and dynamic commercial and economic policies;
- “(2) the creation of an international mechanism for the orderly conduct of foreign exchange operations;
- “(3) the creation of an international institution through which the tendency of the flow of foreign capital to take a cyclical pattern may be counteracted;
- “(4) international action for the solution of the problems of primary production; and
- “(5) the international co-ordination of national policies for maintaining a high and stable level of employment.”³

We are directly concerned in this report with the first point only. But let us be clear that the purpose of freer trade policies is not simply to secure a greater international exchange of goods for its own sake. It is an integral part of the policies for overcoming the scourges of unemployment, under-employment and poverty.

3. *The Importance of a World-Wide Trading System*

Clearly anything short of a world-wide trading system means a restriction of the advantages to be derived from international ex-

¹ *Economic Stability in the Post-War World*, p. 242.

² *Ibid.*, p. 279.

³ *Ibid.*, p. 280.

change. But the re-establishment of effective multilateral trading is important for other reasons. To quote from a recent study by the League of Nations Secretariat:¹

“Modern civilization is based on a world economy which functions through a system of multilateral trade of a specific pattern that embraces the whole world. The present war, and particularly the reduction of British overseas investments, is likely to modify that pattern in the future. But the need for a world pattern of multilateral trade will remain as long as climates and geological deposits continue to vary from one area to another, as long as the factors of production are unevenly distributed over the face of the globe.”

Countries whose exports are largely concentrated on one or a few commodities are not likely to require the particular products of other countries in exactly the proportions in which these countries require their products. The same is true of trade between countries with a more diversified trade; it is only less obvious.

It is essential therefore that multilateral trading, which was severely restricted in the 'thirties, should be restored. It is indeed only under conditions offering ample scope for such trading that countries can satisfy their diverse needs and—in the words of the Atlantic Charter—that “all nations, great and small” can enjoy “access . . . on equal terms, to the trade and to the raw materials of the world needed for their economic development”.

Moreover, any widespread recourse to “bilateralism” or other forms of trading relationships involving discrimination against third parties would involve not only the immediate danger of engendering trade warfare but also the ultimate risk of sapping the bases of political co-operation between peoples and consequently of world peace.

A world-wide trading system must naturally be one that embraces all countries irrespective of the manner in which their economy is organized. All countries in fact have an interest in the development of active multilateral trading and there is none that cannot contribute to that development. The existence of a general trading monopoly in any country does not preclude it from following an expansive rather than a restrictive policy in regard to imports or from promoting international economic integration—the action required of it in order to fulfil the general principle of reducing trade barriers. But the growth of State and State-controlled trading has raised technical problems of considerable difficulty in connection with guarantees of

¹ *The Network of World Trade* (Series of League of Nations Publications, 1942. I.I.A.3.), p. 10.

non-discrimination. We shall briefly consider these problems in Chapter V.

4. *The Central Principles of Post-War Policy*

The two main principles of agreed action in regard to post-war commercial policy to which many of the United Nations have pledged themselves are "the reduction of tariffs and other trade barriers" and "the elimination of all forms of discriminatory treatment in international commerce". We shall discuss these principles separately, but it must be clearly understood that they are interdependent. Trade restrictions are often imposed in retaliation for, or as a defence against, discrimination. More important, discriminatory treatment exists largely because of the trade barriers of certain countries; its removal and the reduction of those barriers must thus proceed *pari passu*.

For the same reason, the application of these principles does not necessarily imply equivalent action by all countries. What is required is a general co-operative effort towards which all countries will make their appropriate contribution. In view of the differences not only in the degree and types of restriction and discrimination found in different countries but also in their balance of payments situations, the nature and extent of the appropriate national contributions will in fact vary widely. Moreover, upon any country in a strong creditor position will fall the responsibility of taking the lead.

The key position of the United States in this respect has been well brought out in the following official statement:¹

"Many countries will feel that they cannot venture to commit themselves to the kind of international economic policy envisaged in Article VII unless they can be reasonably certain that the United States can be counted on to give these principles full support. They look for

¹ Hon. Dean Acheson, United States Assistant Secretary of State: Department of State *Bulletin*, December 3rd, 1944.

The point has been argued from another angle by the United States Under Secretary of Commerce, Hon. Wayne C. Taylor:

"A world economic structure organized on the basis of equal treatment and with large scope for free enterprise cannot be maintained in the face of such reductions in the supply of dollars as have occurred in our international transactions in the past. Unless the supply of dollars is more adequate to meet foreign requirements, other countries will assuredly insist on their rights to exercise a close selective control over the use of the amounts available and to promote more intensive relations with other countries under preferential trading arrangement. Unless dollars are made available with greater regularity than in the past, it would be both unjust and unwise to demand the removal of restraints and controls largely designed to protect the internal economies of other countries against external shock and pressure." (*The United States in the World Economy*, United States Department of Commerce, 1943, Introduction, p. vi.)

some assurance that this country will stand ready through the processes of trade and investment to make available to them goods that they will need; that we will maintain a high level of prosperity in this country and reduce our own obstacles to trade, so that they may have prospects of making repayment for the goods we sell to them. If we give this assurance and join with them in the maintenance of stability in the foreign exchanges, essential to both investment and trade, then there is every prospect that they will be willing to join with us in these measures upon which depend the prospects of an increasing and stable prosperity throughout the world."

CHAPTER IV

THE REDUCTION OF TRADE BARRIERS

I. Adaptation to Changes in International Financial Structure

It was argued in the last chapter that, as part of the co-ordinated drive towards securing higher living standards and greater economic security, commercial policies require to be not only liberal but also dynamic. The first condition of a dynamic commercial policy is that it should adapt itself to fundamental changes in the structure of balances of payments. As a result of the war, great changes have occurred in the international structure of claims and indebtedness. Several countries which have lost or are in process of losing foreign assets and other sources of income and have incurred foreign debts will be obliged to raise the level of their exports permanently and very substantially above the pre-war level if they are to avoid a drastic curtailment in their imports. In the case of the United Kingdom, the increase in exports above the pre-war level which will be required to maintain the pre-war level of imports is understood to be about 50% at pre-war prices. How rapidly and how successfully this adjustment can be effected will depend in part upon the ability of these countries to compete effectively in foreign markets; it will depend still more upon the degree in which those markets can be expanded.

The deterioration in their financial position has its counterpart in the strengthening of the capital balances of other countries, which will be able to import more goods at any given level of exports after the war than they did before. If these other countries substantially increase their imports, they will facilitate the maintenance of imports—and of liberal commercial policies—elsewhere. If they do not, strains will be caused which will very seriously impede the development of a stable and liberal system of trade relationships.

An increase in their imports, to quote again the Delegation on Economic Depressions,¹

“will not . . . cause any contraction of business opportunities at home compared with what they were before the change in the international debt situation. In fact, the national income of these countries has been benefited to the extent of the change in debt services; some consumers' incomes have been raised; if this increase in their income is spent abroad they will not on that account have less to spend at home than they had. On the contrary, if foreign goods are not allowed

¹ *The Transition from War to Peace Economy*, pp. 101-102.

to enter in greater quantities, it may prove impossible to maintain exports in the long run and the whole domestic economy, directly distorted by the war, will be further distorted by failure to adapt to these international changes likewise caused by the war.”

Strong creditor countries will need to maintain a high level of foreign investment to effect an orderly transition from war to peace economy and to prevent a drastic curtailment of employment in their export industries. This will also help in the restoration of world trade and will serve to mitigate payment difficulties in the countries whose contribution to the war has weakened their financial position. But since it will tend further to strengthen the creditor position of the lenders and increase the liabilities of the borrowers, foreign investment represents no permanent solution of those difficulties. Indeed not only are capital exports no substitute for a courageous reduction of trade barriers by the creditor countries but they actually postulate such action in the long run. However remunerative the purposes to which the loans are put, the necessary transfer on service account can only be effected if the creditors permit their debtors to pay by accepting an equivalent increase in imports from them. The conclusion as regards United States policy has been drawn as follows in a recent study issued by the United States Department of Commerce:¹

“A further reduction in the United States tariff structure beyond that already achieved under the reciprocal trade agreements program . . . is not an alternative but a natural corollary to new investment of American capital abroad in the years of peace ahead.”

2. *Quantitative Restrictions and Exchange Controls*

During the period of transition, we shall be faced with a world in which almost all countries impose quantitative restrictions both on imports and exports and employ exchange controls to check not only movements of capital but also movements of goods.

Most countries faced with a serious scarcity of many essential goods will find it necessary for a time to continue rationing, price controls and export restrictions. But goods which a country normally exports are not likely to remain scarce in the country concerned, and it may be hoped that export restrictions on such goods will not last long after reconversion has taken place. Quantitative restrictions on imports and import licensing systems, imposed in part to prevent a glut of imports at depreciated prices but applied also as a safeguard to the currency, have been most important in the past. In the current

¹ *The United States in the World Economy, op. cit.*, p. 21.

conditions of scarcity, however, such instruments of trade restriction are not likely to be as important as financial restrictions, operated through measures of exchange control.

We recognize that many countries suffering under the impact of the war will have to continue for a period to control the transfer of frozen funds and of capital; but we are concerned about the continuance of the application of exchange control to commercial transactions. Under the Bretton Woods proposals these restrictions on current transactions are to be withdrawn as soon as possible by progressive stages. We fully approve of this provision since exchange control applied to transfers on current account, however equitably it is applied, is scarcely reconcilable with a multilateral non-discriminatory trading system. Experience has shown that both quantitative restrictions and exchange controls applicable to current transactions involve a number of disadvantages and dangers which may be summarized as follows:

(i) they insulate national prices and consequently prevent the operation of the world price mechanism in respect to the goods they cover;

(ii) they lend themselves more effectively than ordinary import duties to the application of arbitrary methods of controlling foreign trade;

(iii) they introduce administrative complexities which tend to reduce the total volume of trade;

(iv) being subject to change at administrative discretion, they are an element of instability in trade relationships;

(v) as they cannot be satisfactorily reconciled over a long period with the principle of m.f.n. treatment, they involve the danger of raising international economic rivalries and conflicts to the political level;

(vi) because of the relative disadvantage in which countries without a direct system of trade control are often placed, or as a result of retaliation for abuse of the arbitrary power they afford, they tend to spread and thus finally to react upon the trade of the country applying them, reducing the aggregate proceeds of its exports.

Naturally, the general effects of quotas and exchange controls on international trade as compared with those of tariffs depend upon the degree of restriction or the liberality with which these alternative instruments of trade regulation are applied. Certain countries have recently devised methods to meet some of the most serious disadvantages associated with exchange control in the past. But for the reasons given above, there can be little doubt that the first object of

the commercial policy of countries anxious to foster free individual trading and a world price economy should be to reduce substantially the scope of quantitative restrictions and exchange control as soon as the maladjustments caused by the war have been overcome. Special grounds will continue to exist for the permanent retention of certain-specific state controls (e.g. on narcotic drugs) and such controls may be needed in connection with inter-governmental commodity arrangements. But, with the progress of economic reconstruction and the development of world economic activity, the post-war need for any widespread system of state trading or any extensive quota system should diminish. The restoration of an international monetary system and the establishment of adequate credit arrangements should help to make possible the abandonment of exchange control in respect of commercial transactions.

So far as quantitative restrictions and exchange controls continue to be employed (for instance, to protect balances of payments) the aim should clearly be to make their application as liberal and non-discriminatory as possible. We deal with certain aspects of this problem in the next chapter.

Where quantitative restrictions—and especially quotas—serve to protect national industries, and are not imposed simply to prevent or check the purchase of unessential goods, some alternative form of protection may be considered necessary when these restrictions are removed. But if quantitative restrictions are merely to be replaced by increased tariffs which have an equally restrictive effect, little if any advantage will be gained. How can this danger be avoided?

3. *The Risk of the Replacement of Quantitative Controls by High Tariffs*

What happened after the last war was that many European countries, uncertain of their power to compete in world markets, and having few commercial treaties and still fewer, if any, long-term treaties, substituted very high tariffs for their quantitative restrictions. Of these high tariffs some were due simply to fear, some to the short-sighted conviction that a high tariff afforded a stronger bargaining position when commercial treaties were being negotiated. High tariffs bred high tariffs. Europe entered upon a phase of "*tarifs de combat*".

A number of conditions will, we believe, determine the possibility of overcoming the danger we have in mind:

(a) If countries are successful in bringing about high levels of economic activity and employment, of applying, that is, expansionist

policies, the element of fear which proved so important in the early 'twenties will be largely removed. "It is only under conditions of active home demand and full domestic employment that countries can be expected to welcome imports and to regard their exports, not as a means of providing employment, but as an inevitable cost of the goods desired."¹ But a generalized state of high economic activity throughout the world is, for the reasons we have already explained, only likely to be secured if there has been a substantial reduction of war-time obstructions to trade—a large increase, that is, in the size of the admitted quotas while quantitative restrictions are still in force.

(b) Much will depend upon the degree in which the "unique opportunity . . . for choosing those lines of production that can stand on their own feet without heavy tariff protection or subsidies"² can be seized in connection with the post-war reconversion and reconstruction of industry. Moreover, now and for some time after the war there will be a scarcity of goods in most countries and the immediate need will be to eliminate protective tariffs or quantitative restrictions which impede necessary imports, subject to such measures of exchange control as are needed to safeguard the balance of payments. This situation should give governments an opportunity, which will not recur, to adopt more liberal trade policies. Some governments have already taken steps in that direction.³

(c) It is much to be hoped that these national programmes of re-adaptation will not be left to be worked out by each government independently. The revival of trade activity will be greatly assisted if some procedure can be developed for international consultation and planning, not as regards commercial policies only, but also as far as practicable as regards the adaptation of production in the reconstruction period.

(d) The necessary adaptation may be seriously impeded unless steps are taken to prevent vested interests in the maintenance of import controls, tariffs and other trade barriers from developing during the transition period, as they did after the last war. We discussed in our last report⁴ the methods by which the danger of abnormal profits being derived by traders from the granting of licences for import or

¹ League of Nations: *International Currency Experience* (Series of League of Nations Publications, 1944.II.A.4.), p. 208.

² Hon. Cordell Hull, United States Department of State *Bulletin*, Volume X, No. 256, May 20th, 1944.

³ For example, France has entirely suspended her import duties and Belgium part of hers.

⁴ Economic and Financial Committees: *Report to the Council on the Work of the 1943 Joint Session* (Geneva, doc.C.I.M.I.1944.II.A.).

export might be overcome. The problem of preventing the growth of vested interests among producers is more serious since the investment of additional capital in fixed plant (a consideration of great importance in view of the scarcity of capital in many countries) and the training and employment of additional workers are involved; it also presents greater difficulties. A memorandum on the subject by the Economic, Financial and Transit Department is annexed. (Annex II.)

These are the four major conditions, we believe, for avoiding the danger of quantitative controls being succeeded by no less restrictive tariffs. Two complementary routes towards the goal of freer trading present themselves, namely, autonomous and contractual action.

4. Autonomous and Contractual Action

The need, which we discussed at the beginning of this chapter, for adapting commercial policy to the great structural changes produced by the war can only be met by radical and courageous measures, in which the countries whose creditor position has been strengthened must be prepared to take the lead. It would be a mistake to accept the view that modifications in trade positions can only be effected as the result of a contractual bargain. Much can be done by spontaneous action by individual countries—action which might be encouraged were guiding principles such as the following generally accepted, subject to such exceptions as might be considered indispensable:

(a) that protective duties which do not protect any existing industry should be removed and that protection should be withdrawn¹ from any industry which supplies an insignificant proportion of the national consumption of its product;

(b) that in respect of any industry with tariff (or equivalent) protection above a given level—which would vary according to the general scale of the country's tariff—(i) reports should be published by the national tariff authorities at regular intervals upon the measures taken by the industry to reduce prices and costs (which should, however, not involve wage reductions out of line with the general level of wages in the country) and to improve the quality of its products; (ii) the protection to be accorded should be periodically reconsidered on the basis of these reports.

But the main hope of securing a general demobilization of tariffs

¹ See Eugene Staley: *World Economic Development*, International Labour Office, Montreal, 1944.

will clearly lie in the conclusion of trade agreements, bilateral or multilateral, under which immediate risks attending upon the removal of a given trade "defence" are offset by immediate openings for exports.

The United States Trade Agreement programme may well remain one of the principal instruments of such action. That programme itself has, moreover, mitigated the objection sometimes raised by other States to tariff reduction by contractual action, namely, the reluctance to make concessions which would automatically be extended to high-tariff countries that refused to make concessions themselves.

We believe that the *tempo* of bilateral negotiations should—and could—be more rapid than in the past. Much will depend, naturally, upon the adequacy of international and national administrative machinery; but certain developments in procedure may contribute. A programme of linked negotiations under the guidance of an international body has been suggested in Chapter II.

It will be more difficult than in the past to deal separately with tariffs and quantitative restrictions; as a rule both will no doubt have to be considered together. Moreover, while the immediate objective should be to secure international agreement there will be scope for agreement between those countries that are ready to agree or between "key" countries upon whose action that of the rest of the world will largely depend.

5. *The Impact of the Industrialization of Undeveloped Areas*¹

We have said above that the goal of a more satisfactory trading system is not likely to be reached rapidly, and we must remember that the trade within that system will be constantly shifting and changing in composition. We must think in terms of a dynamic world, in which all countries will increase their productive capacity. The less developed countries will be anxious to raise their standards of living by pushing forward their industrialization as rapidly as possible. The importance of these changes to the under-developed countries themselves and to world security and economic stability have been discussed in the report of the Delegation on Economic Depressions.²

It is clearly in the interests of both the older industrial countries and those anxious to industrialize and diversify their economies (I)

¹ A detailed analysis of the effect of industrialization upon international trade since the 1870's has been undertaken by the Economic, Financial and Transit Department of the League. We trust that this analysis will shortly be published.

² *Economic Stability in the Post-War World*.

that the latter countries proceed with due reference to local resources and comparative cost advantages; (2) that there should be some international consultation in regard to the effects of these developments on commercial policies.

As has been said in another recent League report,¹ when discussing the fact that the expansion of industries in backward areas may be so rapid as to render adaptation in other countries to changing competitive conditions extremely difficult and painful:

“There is no single simple solution of this problem. It will present itself in different forms at different times and to different countries. Some cushion against the incidence of too rapid change may be required. But there would, we believe, be a very real advantage if, instead of leaving this problem to be settled when it arises by unilateral action, it could be discussed by an international body which would review it in all its aspects and tender advice to governments.”

Such a body would, of course, serve a much wider purpose than that of helping in the solution of this particular problem, and its value would not be confined to the two types of countries we have been considering.

6. *Administrative and Legal Barriers*

Apart from tariffs, subsidies and quantitative restrictions, there are innumerable varieties of administrative and legal measures which act as potent barriers to trade. The evils of some—for example, excessive customs formalities and double taxation—lie in the uncertainties, the vexations and the burdens they impose on traders and foreign enterprises. Our experience has shown that international action to remove or reduce such barriers can count on much general support, and more important, little opposition; and a basis for further action exists in the work accomplished through the League.

More difficult to counter are measures of “administrative” or “indirect” protection which grew considerably in importance in the 'thirties. Many countries have introduced, for example, sanitary restrictions on the importation of animals, meat and plants, statutes and regulations designed to protect business against “unfair” competition, against abuse of patents and copyrights, etc., which can be, and frequently are, used as instruments of economic protection. Protection by such means is the more dangerous because it is concealed from the public and subject to administrative discretion. We believe that the most promising international approach is to devise rules for general

¹ *The Transition from War to Peace Economy*, p. 107.

adoption embodying the maximum guarantees which importing countries are justified in requiring from exporters. Irrespective of international action, national action with a view to limiting sanitary and other regulations of the kind we have been discussing to their legitimate purposes is, however, obviously desirable.

7. Customs Practices

There are a number of measures concerning tariff practice and technique that would be likely to facilitate commercial operations or the conclusion of commercial treaties.

(a) The first of these is the standardization and simplification of Customs Nomenclature. As we have mentioned in Chapter I, a draft Standard Nomenclature prepared by the League is in existence and has already been applied by many countries.

(b) The second is the replacement, so far as practicable, of specific by *ad valorem* tariffs. Specific tariffs have the dual disadvantage (1) of not taking account of changes in relative prices and values and hence tending to encourage higher duties as a precaution against a rise in unit values, and (2) of increasing the incidence of the tariff in periods of falling prices.¹

(c) Non-negotiable tariffs, or narrow legislative limits to the percentage cut in duties that can be offered in return for reciprocal concessions, stand in the way of agreements for tariff reduction. We would favour the replacement of such non-negotiable tariffs as remain by negotiable tariffs and the granting of the greatest possible freedom for tariff reduction by contractual methods.

(d) In many countries, owing to administrative and legislative survivals, responsibility for the formulation and application of commercial policy is divided and producer interests are allowed to exercise an undue influence upon such policy. It would seem very desirable that responsibility for commercial policy should be centralized and the responsible authority so constituted that divergences between commercial and general economic policy may be avoided.

¹ On the business-cycle aspects of this question, see *Economic Stability in the Post-War World*.

CHAPTER V

NON-DISCRIMINATION

1. *The Importance of M.F.N. Treatment*

For the development of a stable peace-time system of trade relations, the restoration of conditions ensuring effective equality of treatment for the commerce of all nations is as essential as the reduction of trade barriers. In the long run, countries will be no more willing in the future than they have been in the past to submit to measures in other countries which they consider to be directed specifically against their exports or traders, which arbitrarily accord to the exports or traders of other countries special advantages that their own do not enjoy, or which cause them to pay more for their imports than others are required to pay. The aim should be to secure, together with "the reduction of tariffs and other trade barriers":

(a) the fullest and widest application of the unconditional m.f.n. clause in customs matters as well as in the treatment of foreign nationals and firms;¹

(b) the removal of preferences or the application of preferential systems only in accordance with agreed principles of policy;

(c) the abandonment of discriminatory currency measures, except as and when permitted by international authority;

(d) effective equality of treatment in the application of internal fiscal or other regulations affecting imports or exports;

(e) the allocation of quotas (including foreign exchange quotas, where adopted) on as equitable a basis as possible between foreign countries;

(f) the operation of state trading monopolies according to non-discriminatory principles;

(g) the removal of discriminatory tariff classifications;

(h) the suppression so far as possible of "unfair competition" and discriminatory practices by private cartels or monopolies.

All these objectives are of importance, for where any form of discrimination exists, justification can be found for discrimination in other countries on grounds of retaliation or self-defence. A period of transition may be required for the removal of certain discriminatory measures pending the easing of strains on national balances of pay-

¹ See, however, Section 5 below concerning the question of a "low tariff club".

ments and the general expansion in the world consumption and exchange of goods. None the less, every effort should be made to secure the maximum equality of treatment possible.

The movement in this direction would be expedited and facilitated and much possible controversy avoided if there were general agreement on principles. Our recommendations on the form, the field of application and the interpretation of the m.f.n. clause in Customs matters drawn up between 1927 and 1931, might form a basis for such an agreed doctrine. As mentioned in Chapter I, they are attached to this report for reference. But they do not cover the entire field of relationships in which equality of treatment should be ensured; and they will no doubt require amendment and expansion to meet problems that have since come to the fore—in particular those arising from the relationships between free-market and controlled economies.

At this stage we shall confine ourselves to making some suggestions concerning individual problems. Let us first consider how the danger of discriminatory treatment through the application of quotas and monopolies may be reduced.

2. M.F.N. Treatment and Quotas

As we pointed out in a report issued in 1936,¹ “no system has been discovered by which quotas can be allocated without injuring the interests of countries entitled to benefit under the most-favoured-nation clause.” We added that the proportional method—that is, allocation between supplying countries in proportion to the imports received from them in a “representative period”—was “the only one which can ensure as equitable an allocation as the existence of quotas allows”.

Allocation of quotas or foreign exchange on the basis of imports in a representative period naturally tends to freeze an obsolescent and increasingly arbitrary *status quo* and prevent changes in competitive conditions from working themselves out in the currents of trade. After the war, the changes in competitive conditions will be so vast that it is very doubtful whether any pre-war year or period of years could serve as a basis. Allocations will have to be negotiated and the danger of discrimination will be at a maximum. In these negotiations we suggest that rules along the following lines, proposed in a recent League of Nations publication,² might usefully be made standard

¹ *Equality of Treatment in the Present State of International Economic Relations: The Most-Favoured-Nation Clause* (Geneva, doc.C.379.M.250.1936.II.B.), p. 14.

² *Trade Relations between Free-Market and Controlled Economies*, by Professor Jacob Viner (Geneva, 1943), pp. 68-69.

practice to supplement the "representative period" formula as applied to quotas:

"(a) there should be no secret quotas;

"(b) the basis upon which quotas have been allocated should be made public at the same time as the quotas are announced;

"(c) the allotment of quotas as between countries should be retained as a governmental function and should not be delegated or be permitted to be exercised by any non-official agency such as a cartel or trade association;

"(d) whatever basis is used in allotment of quotas to any country in accordance with the 'representative period' formula should not be inherently incapable of extension to at least all the major foreign sources of supply of the particular commodity involved;

"(e) in trade agreements countries should agree not only not to discriminate against each other in their own quotas, but also not to seek preferential quotas in third countries for commodities in which the other country also is interested as an exporter."

This last point is of course of great importance. Discrimination was promoted in the 1930's by countries which, while preserving equality of treatment in their own import practice, negotiated concessions from other countries that could only be granted at the expense of third parties.

3. *M.F.N. and State Trading Monopolies*

Most of the above rules embody objective criteria and their observance or non-observance can be checked, if not immediately, at least after a period of time. State trading monopolies present the special problem that no formulae embodying such criteria appear to be available. It has been a common practice to give an exact pledge of fair and equitable treatment by trading monopolies. The following are among the provisions that have been used in this connection by the United States:

"In the event that (either Government) establishes or maintains an official monopoly or centralized agency for the importation of or trade in a particular commodity the Government establishing or maintaining such monopoly or centralized agency will give sympathetic consideration to all representations that the other Government may make with respect to alleged discriminations against its commerce in connection with purchases by such monopoly or centralized agency.

"In case of a Government monopoly for import, production or sale . . . the Government . . . agrees that in respect of the foreign purchases

of such monopoly or agency the commerce of the other country shall receive fair and equitable treatment.

"To this end it is agreed that in making its foreign purchases of any product such monopoly or agency will be influenced solely by those considerations, such as price, quality, marketability, and terms of sale, which would ordinarily be taken into account by a private commercial enterprise interested solely in purchasing such product on the most favorable terms."¹

In case of differences of opinion as to the carrying out of such pledges, the existence of an international machinery providing for (a) consultation, (b) objective appraisal of the facts and (c) mediation, or if necessary, arbitration, should be helpful.

4. *Non-discrimination in Certain Other Fields*

Exchange Control: Where exchange control continues to be enforced in respect to commercial transactions, it would seem desirable that regard should be had, so far as possible, to past distribution of trade. The same safeguards in connection with the representative period formula as were suggested in the case of quotas might usefully be adopted *mutatis mutandis*.

It is, however, often the very purpose of exchange control to limit allocation of particular foreign currencies which are in short supply. The contingency of a particular currency becoming generally scarce has been provided for under the Articles of Agreement relating to the International Monetary Fund (Article VI, Section 3) whereby any member country is expressly authorized "after consultation with the Fund, temporarily to impose limitations on the freedom of exchange operations" in a currency which the Fund has formally declared to be a scarce currency. It is to be hoped that international equilibrium will be well enough maintained to obviate the need for recourse to such measures; but should it be necessary, the provision embodied in the Bretton Woods proposals that action must depend upon decision by the Fund—in which the country against whose currency the action is directed would participate—is clearly of great importance.

These measures do not of course meet the case of a country finding itself short of a currency which is not generally scarce. Such a case may arise so long as currencies are not generally interchangeable. It is, however, the object of the Bretton Woods proposals to create conditions permitting such general interchangeability.

¹ *Trade Relations between Free-Market and Controlled Economies, op. cit.*, pages 79-80.

Administration Regulations: Discrimination in the application of administrative or legal rules affecting imports, designed to protect consumers or patentees or imposed on sanitary grounds, may be met by the methods we suggested for avoiding concealed protection to domestic producers through such rules. The aim in most cases is to render specific the pledges in such matters normally extended under the m. f. n. clause in commercial treaties.

Treatment of Foreign Nationals and Firms: M. f. n. pledges concerning the treatment of foreign citizens and firms of different nationalities are of great importance to the development of co-operative economic relationships. It is very desirable that governments should refrain from seeking special advantages in foreign markets for their nationals and firms. But they can scarcely be expected to do so unless the rights and status to be enjoyed under a system of equal treatment are adequate.

The most favourable treatment accorded by some countries involves serious discrimination against all foreigners and foreign firms, or exposes them at any moment, at the discretion of the authorities, to the loss of whatever rights they may enjoy. Apart from other evils, such a situation is an effective bar to foreign investment, and it is frequently found precisely in those areas most in need of foreign capital for their economic development. Wherever practicable, the aim should be to obtain for all foreigners a status approximating to "national treatment", and specific guarantees such as are indicated in the Draft International Convention on the subject which we put forward in 1929.¹

5. *M.F.N. and the Reduction of Trade Barriers*

So far we have been discussing how national measures affecting the trade or traders of other countries may be applied in a non-discriminatory manner. Let us now look at the problem of non-discrimination a little more broadly with reference to other major objectives of post-war economic policy.

Clearly an over-rigid insistence on the m. f. n. principle should not be allowed to stand in the way of a reduction of trade barriers. As we observed in 1929,² if there are to be collective trade agreements for the latter purpose "of a general character and aiming at the improve-

¹ *International Conference on the Treatment of Foreigners. Preparatory Documents* (Geneva, doc. C. 36. M. 21. 1929. II.).

² *Recommendations of the Economic Committee Relating to Commercial Policy, op. cit.*, p. 13.

ment of economic relations between peoples", those States which decide to remain outside and pursue restrictive policies cannot be permitted to share in the benefits mutually accorded to one another by the parties. We recommended that an exception to m.f.n. treatment should be admitted in favour of such agreements, and a so-called "multilateral clause" based on our recommendations was in fact extensively used in continental European treaties in the following years. That clause is to the following effect:

"... The m.f.n. clause cannot be claimed by the High Contracting Parties to obtain new rights or privileges that may in the future be granted by one of them in collective conventions to which the other High Contracting Party is not a party, if the said conventions are concluded under the auspices of the League of Nations or registered by it and open to the accession of all States. However, such rights or privileges can be claimed by the High Contracting Party interested (*i.e.*, the other Party), if the said rights or privileges are laid down also in conventions other than the collective conventions satisfying the above conditions, or, further, if the High Contracting Party claiming to enjoy them is prepared to grant reciprocity of treatment."¹

An attitude similar to our own was taken at the Seventh International Conference of American States held at Montevideo in 1933 and was embodied in the International Convention deposited in Washington in 1934. The type of multilateral agreement whose benefits would constitute an exception to the m.f.n. clause, is defined in Article 1 of that Convention; it should:

- (a) be general in application,
- (b) include a trade area of substantial size,
- (c) have as its objective the liberalization and promotion of international trade or other international intercourse, and
- (d) be open to adoption by all countries.

A proviso (Article 2) was inserted to the effect that a non-party State may claim m.f.n. treatment for herself if she, in fact, accords the benefit so claimed to all party States.

It must be admitted, however, that general provisions of the type above mentioned may sometimes be difficult of interpretation and application in practice. For example, an agreement between a particular group of countries might be beneficial to their mutual trade but not in the interests of international trade as a whole. In any event, it

¹ Translation from the French. Switzerland-Belgo-Luxemburg Treaty of August 26th, 1929.

would seem desirable that any initiative taken for reducing barriers to international trade by this method should be arranged under the auspices of an international economic authority and command the support from the outset of a really substantial nucleus of countries; otherwise there would be a serious risk of stimulating non-adherent countries to adopt counter-measures rather than to associate themselves with the initiative.

We discuss in the next chapter the more difficult problem of agreements of a less general character for creating freer trade within specific areas, as well as the manner in which certain practical problems, which involve the principles not only of freer but also of more equal trade—cartels, commodity regulation schemes and obstacles to the supply of raw materials—might best be approached.

CHAPTER VI

SPECIAL PROBLEMS

I. *Customs Unions, Regional Agreements, etc.*

After the last war, some restricted provision was made for the conclusion of special Customs arrangements between certain of the new and truncated countries of Europe which had previously formed part of a single free trade area. But the matter was not pressed for some years and vested interests and nationalist sentiment within the countries concerned soon acquired sufficient influence to prevent agreements from being reached. In the 'thirties, the creation of limited freer trade areas and special Customs arrangements initiated on a regional basis were proposed by various countries. Some such agreements were concluded, but others encountered opposition and had to be abandoned. The absence was felt of an agreed body of principles concerning admissible exceptions to the m.f.n. clause and of an international body to which the proposals could have been referred. It may be hoped that if wider international action can be taken on the lines recommended in this report there will be less occasion for special regional arrangements; but insofar as special Customs arrangements are considered desirable in specific areas after this war, we suggest:

- (a) that they should be created at an early stage;
- (b) that the existence of (1) a body empowered to tender advice to governments upon any proposals involving a derogation from m.f.n. treatment, and (2) agreement on safeguarding principles, would be valuable. We set out below some general considerations concerning the principles that might be appropriate.

*Customs Unions*¹: Full Customs Unions "constitute exceptions, recognized by tradition, to the principle of most-favoured-nation treatment".² This does not mean that third parties may not oppose the formation of any given Union. Political consequences may be implied—as happened in the case of the proposed Austro-German Customs Union of 1931—which give rise to apprehensions abroad. Furthermore, even assuming that the Union tariff does not average higher than the existing tariffs of the parties, a change in the tariff schedule of any party likely seriously to harm the trade of particular countries

¹ For countries contemplating a customs union, special problems in connection with the avoidance of the growth of vested interests behind quantitative restrictions present themselves. These problems are briefly discussed in Annex II (Note by the Secretariat), pp. 115-117.

² *Recommendations of the Economic Committee Relating to Commercial Policy*, op. cit., p. 11.

may well provoke opposition to the Union. But where such political or economic objections are absent or can be overcome, and where the adoption of a common tariff promises a real economic advantage to the countries concerned, it would seem altogether desirable that Customs Unions should be fostered.¹

The cases in which a Customs Union could be brought about at one stroke are bound to be very limited. In most cases the parties would have to proceed by stages in order to soften the impact of the changes on their economy. While the Union was in process of formation, therefore, there would exist a preferential regime between the parties to it conflicting with their m.f.n. obligations. But in spite of this fact, it is, we believe, widely held that a temporary waiver of m.f.n. rights by third parties to permit the gradual formation of a Customs Union unobjectionable on political and economic grounds would be justified where the parties can show :

- (a) that the Union is genuinely intended, and
- (b) that appropriate steps are being taken to realize it within a specified and relatively short period of time.

If an international economic authority is set up, it would appear particularly appropriate that all proposals of this kind should be submitted to it for consideration.

Regional Preferential Arrangements: A number of "regional" exceptions to the m.f.n. clause—for example, the Iberian clause, the Baltic clause, the Scandinavian clause, the Central American clause, etc.—have been widely conceded on the ground of the special ethnic, historic, geographic or other ties uniting the countries concerned. We feel however that the question of extending the number or scope of such exceptions or of recognizing new permanent regional preferential arrangements should be approached with caution.

Recommendations on the subject were made by various international bodies in the 'thirties, when the hopes of general tariff reduction had been frustrated and the multilateral system of settlements had largely broken down. Thus in 1931 the Sub-Committee of Economic Experts of the Commission of Enquiry for European Union recommended the conclusion of limited group agreements subject to the following conditions:²

¹ In exceptional cases, reciprocal free trade in indigenous products may be considered between neighbouring countries. As an example of such arrangements may be mentioned those reached between certain Central American countries in the inter-war years. These agreements come within the Central American exception to m.f.n. treatment.

² *Commission of Enquiry for European Union, 1931, Fourth Session, League of Nations Document (C.681.M.287.1931.VII.). Annex 2, p. 42.*

“(a) The groups of countries which they affect should be such as to ensure that they are in conformity with the general interest and contribute to the general progress of Europe;

“(b) They must not injure the interest of other countries, but must, on the contrary, tend to encourage economic intercourse with them;

“(c) They must as far as possible include the free movement of individuals, goods and capital, and indeed all forms of economic activity, so that a fair balance may be established between sacrifices and advantages;

“(d) If they lead to treaties or agreements different from the ordinary commercial treaties:

(1) These must be open to accession by all countries prepared to conform to the obligations which such treaties or agreements entail;

(2) They must provide for the granting of the stipulated advantages to non-signatory countries which accord equivalent advantages, whether by treaty or by virtue of their own autonomous policy.”

The Preparatory Committee for the International Monetary and Economic Conference of 1933 suggested that, if multilateral tariff agreements were impracticable, agreements among a group of countries should be attempted and an exception to m.f.n. treatment admitted in respect of such agreements, provided that they conformed to certain conditions, e.g. that they did not involve “new hindrances to international trade *vis-à-vis* countries having most-favoured-nation rights”.¹ A similar recommendation was made by M. van Zeeland in his report to the British and French Governments in January 1938.²

Acting upon a recommendation by the Montevideo Conference of 1933, the Inter-American Financial and Economic Advisory Committee worked out a formula in September 1941 under which arrangements of this kind might be permitted within the framework of the general m.f.n. principle, and approved the following recommendations (Resolution XXIII) :

“That any such tariff preferences, in order to be an instrument for sound promotion of trade, should be made effective through trade agreements embodying tariff reductions or exemptions;

“That the parties to such agreements should reserve the right to reduce or eliminate the customs duties on like imports from other countries;

“And that any such regional tariff preferences should not be per-

¹ *Draft Annotated Agenda of the Monetary and Economic Conference* (League of Nations Document C.48 [1].M.18 [1]. 1933.III.).

² Cmd. 5648.

mitted to stand in the way of any broad program of economic reconstruction involving the reduction of tariffs and the scaling down or elimination of tariff and other trade preferences with a view to the fullest possible development of international trade on a multilateral unconditional most-favored-nation basis."

This formula would naturally require to be supplemented by safeguards concerning preferences by means other than tariffs. No formula, however, can cover all cases that might arise. Governments will be chary of renouncing their rights to determine their attitude toward any specific proposal on its merits. Hence the importance of objective scrutiny and report by an international body, as suggested above.

2. *Private Trade Restrictions*

The condemnation of discriminating monopoly and of restrictions upon international trade which cut across the rational and orderly development of the world's productive resources applies not only to action by States but *a fortiori* to action by private cartels, which has the added disadvantage that it is not only conceived in a sectional interest but escapes control in the public interest.

Outright prohibition of international cartels might in some cases require a far-reaching system of State control over the operation of industry which would tend to defeat the aim in view; and there is reason to believe that such prohibition would be largely ineffective so long as world markets are disorganized and the regulation of competition remains a condition of avoiding serious unemployment in certain national industries. Governments have frequently used measures of commercial policy to strengthen the position of national industries in international cartels. A general renunciation of this practice should clearly be aimed at; but this again is an objective that could scarcely be realized until the urgent problems of maladjustment which give rise to such intervention are overcome. A programme of the following type might, however, be considered:

(a) compulsory and public registration in every country of all such private international agreements in which national producers participate, the information to be supplied covering membership, prospective duration, geographical scope and main stipulations of the agreements;

(b) the information concerning international cartel arrangements thus made available to be communicated regularly to an international body and published by it; this body should be empowered to follow and report on the development and operations of cartels, with particular reference to their effects upon international trade, technical

progress, production, conditions of labour, prices and the supply situation of individual countries ; .

(c) a common code of rules and standards to be drawn up for international acceptance with a view to preventing abuses ;

(d) an international authority should be available to hear complaints from Governments of violations of this code and to facilitate settlement and propose corrective measures, if necessary.

3. *Inter-Governmental Commodity Regulation*

Elimination of violent movements in prices of raw products such as were characteristic of the inter-war period necessarily forms part of the general economic programme of the United Nations and it is a condition of avoiding a resurgence of trade restriction. We consider that measures to reduce fluctuations in the prices of primary products are very desirable and that their successful application would tend to maintain the incomes of producers and hence the purchasing power of countries largely dependent upon the export of primary products. This would make easier the adoption of liberal economic policies by such countries and diminish the risk that "productive capacity which is again vitally requisite during a boom may be destroyed during a depression".¹

In regard to the means which should be adopted for this purpose, the Delegation on Economic Depressions has drawn attention to the desirability of creating an international buffer stock agency with the function of purchasing certain crude products when prices tend to fall and selling them when prices tend to rise.² If such an international scheme can be set up it should diminish the need for international measures to regulate production and trade ; but, as the Delegation itself has recognized, the problems of surpluses in certain commodities, especially commodities whose production in some countries has been vastly increased to meet war requirements, may well be so serious after the war as to require direct measures of control.

The main evils of commodity control schemes in the past have lain in the fact that these schemes have attempted to remedy a situation of surplus production and of depressed prices through restriction of output in a way which tended to preserve rather than eliminate high cost producers and to prevent a desirable transfer of excess capacity and resources into other uses. Furthermore, when schemes have been operated exclusively by producing countries, they have given rise to

¹ *Economic Stability in the Post-War World*, p. 273.

² *Ibid.*, pp. 265-271, 313-314.

apprehensions—and frequently to specific complaints—on the part of consumers.

It is important that in any future inter-governmental commodity arrangements these evils should be avoided. If commodity regulation were to assume the character of monopolistic exploitation, not only would the prospects of raising world living standards be jeopardized but the terms of trade of consuming countries—especially those highly dependent on imports of the controlled commodities—would be seriously affected, while other countries producing raw materials and foodstuffs not covered by regulation schemes might legitimately complain of inequitable treatment.

On the basis of the Report of the League of Nations Committee for the Study of the Problem of Raw Materials, we made the following proposals in 1937:¹

“International regulation schemes should be so framed as to admit effective association of consuming interests with their administration, and to make available adequate information regarding their operation. They should be administered in such a way as to provide consumers with adequate supplies of the regulated material, to prevent, so far as possible, the price of the regulated material from rising to an excessive height and to keep that price reasonably stable.

“In so far as Governments are themselves parties to a scheme, they will of course be responsible for seeing that the scheme is framed and administered in accordance with these principles.

“In so far as Governments are not themselves parties to a scheme, they should be ready, so far as circumstances permit, to use their influence to secure the application of these principles by their nationals parties to the scheme.

“In either event, they should be ready to take all possible steps to ensure the investigation of complaints by other countries in regard to the operation of the scheme.”

Certain further desirable safeguards have more recently been put forward in official quarters:²

(a) The regulation schemes should run for a limited period only, and be subject to revision after review of the situation in the commodity market concerned.

(b) Provisions for the regulation of trade and production should

¹ Economic Committee: *Report to the Council on the Work of its 47th Session* (Geneva, doc.C.577.M.411.1937.II.B.).

² See e.g. International Labour Office: *Intergovernmental Commodity Control Agreements*, Montreal, 1943, and statement on U.S. policy regarding commodity agreements, by Bernard F. Haley, Director of the Office of International Trade Policy, Department of State (*Department of State Bulletin*, April 8th, 1945).

be combined with programmes of (i) technical research with a view to developing the uses to which the commodity may be put and (ii) the elimination of highest cost producers.

(c) Regulation schemes should be closely co-ordinated with other measures of anti-depression policy.

(d) Wherever existing labour conditions are unsatisfactory, there should be arrangements to ensure fair remuneration and other conditions of employment and adequate social security protection to labour employed on the production of controlled commodities.

(e) A body of principles, to which every commodity regulation scheme should be required to conform, should be drawn up for international agreement.

(f) Overall international supervision of the operation of commodity schemes and co-ordination of their policies should be provided for.

(g) For the purposes indicated above, a suitable machinery for international action should be created.

4. *Obstacles to the Supply of Raw Materials*

As we and other League bodies have frequently emphasized,¹ the problem of commercial access to raw materials in peace-time is essentially a problem of payments and its only general and permanent solution lies in the restoration of international exchange on the widest possible basis. Nevertheless the removal of obstacles or potential obstacles to the supply of raw materials is very desirable. Upon request by the League Council, we drew up, in 1937, a series of principles to which it was suggested that "Governments should conform, so far as possible, both in their metropolitan territories and in the Colonies, Protectorates and other territories over which they exercise effective authority."²

The principles proposed that related to international commodity regulation schemes have been mentioned in the last section; the others were as follows:

A. Prohibitions, Restrictions and Duties on the Exports of Raw Materials

1. Raw materials should not be subjected to any export prohibition or restriction except in pursuance of an international regulation

¹ Cf. Provisional Economic and Financial Committee: *Report on Certain Aspects of the Raw Material Problem* (Geneva, doc.C.51.M.18.1922.II.), p. 67; *Report of the Committee for the Study of the Problem of Raw Materials* (Geneva, doc.A.27.1937. II.8.).

² Economic Committee: *Report to the Council on the Work of its 47th Session*, *op. cit.*

scheme, which is being operated in accordance with the principles set out . . . below, or some other international agreement between exporting and importing countries.

2. Raw materials should not be subjected to any export duties except duties imposed at a uniform rate irrespective of the country to which the goods are exported either (a) for revenue purposes, or (b) in order to finance arrangements for improving the production, utilisation or marketing of the raw material in question.

B. Development of Natural Resources

Foreigners should have the same rights and facilities as nationals for developing the natural resources both of sovereign countries and of colonial territories, subject to their obeying the laws and regulations of the countries concerned.

This principle should be introduced by degrees where it is not already in force, and applied as fully as possible.

It is recognised, however, that provisions may be necessary to regulate the conditions of admission and settlement of foreigners and also, in colonial territories, to safeguard the interests of the native inhabitants; but such provisions should not be applied in such a way as to neutralize the possibility of foreign participation nor, in colonial territories, to place nationals of the metropolitan country in a privileged position.

To these principles we added certain riders: that exporting countries could scarcely pursue a liberal policy if the importing countries pursued policies detrimental to their interests, "particularly in such matters as the uneconomic production of substitutes"; that exporting countries could not reasonably be expected to place no export duties on raw materials if the importing countries placed high duties or even prohibitions on the import of processed materials and thereby adversely affected the processing industry of the producing country; that if a country produced only a small quantity of a particular raw material as compared with its requirements, it would not be unreasonable if it felt unable to allow export.

Comments on these proposals were received from ten Governments before the outbreak of war including the United States of America, the United Kingdom, France, the Netherlands, Belgium, and one of the countries that had complained most of difficulties in obtaining raw materials, Poland. While certain additions and modifications were suggested, in principle all these comments were favourable—the United States, for example, stating that it was "prepared to give the

most sympathetic consideration to whatever action is proposed" and being of the opinion that "action in this field should be as far-reaching and as effective as proves to be possible." But the view was generally held that the time was inappropriate for international action. Now, however, the time for such action is clearly at hand and it is hoped that these proposals may be useful as a basis for international discussion.

CHAPTER VII

SUGGESTIONS REGARDING INTERNATIONAL ACTION

1. *The Present Opportunity*

As we have stated in the Introduction, conditions will be far more catastrophic after this war than they were at the end of the last war, and the difficulties of restoring production in many countries or of re-establishing a smooth working system of international trade in the world will prove to be of appalling proportions. The problem of the transition from war to peace economy has been considered in another League report,¹ and we wish to turn our attention here to long-term policies. The present moment, indeed, affords an opportunity for the formulation and adoption of constructive long-term policies which is unlikely to recur for years to come.

First, in view of the great dislocations in the structure of industrial and agricultural production caused by the war, a vast programme of adaptation to peace-time conditions will in any case be necessary. Through appropriate government policies it should prove possible to effect this process of adaptation in such a way as to integrate national economies into one another and to effect a more economical international division of labour and of productive equipment than in the past. In this connection it is interesting to note that the consultative agreement concluded on March 20th, 1945, by Belgium, France, Luxembourg and the Netherlands stipulates that the objects of the consultations proposed will be especially "to harmonize existing production, bearing in mind the traditional flow of trade between these four countries."²

Secondly, most countries are suffering from a scarcity of goods; imports are urgently required, and it should be possible to reduce obstructions to trade without giving rise to opposition from those who in other circumstances might dread foreign competition. There is today, a much stronger desire for imports than is characteristic of normal peace-time conditions; indeed the revival of economic activity in many parts of the world is inevitably dependent on an increasing inflow of goods from abroad.

Thirdly, at the present time in most countries labour is fully employed, or the unemployment that exists is caused by shortages of

¹ See *The Transition from War to Peace Economy*.

² "L'harmonisation des productions existantes, compte tenu des courants commerciaux traditionnels entre les quatre pays."

equipment, of raw materials and of transportation, and not by foreign competition. In the past, fear of unemployment has been an important factor hindering the adoption of liberal trade policies. The increasing recognition by governments of the obligation to maintain a high level of employment may again result in economic nationalism unless the opportunity is seized when employment is at high levels to put liberal policies into effect. Only by such policies can the national pursuit of high employment and the most productive use of the world's economic resources be rendered compatible with each other.

Finally, at the present time there is among the United Nations an experience of co-operation for war purposes and a will to co-operate which, if continued for peace-time purposes, would provide a dynamic force moving the world in the direction of liberal economic policies.

In the past, governments have too often approved recommendations in favour of liberal policies in principle, and in practice raised higher and higher barriers to trade, owing to the pressure of vested interests or to balance of payments difficulties. They have only too frequently exemplified the Latin saying: "*Meliora probo; deteriora sequor*".¹ The present situation demands an effort to break from this unfruitful past and gives an opportunity for putting accepted principles into general practice.

2. *Objectives of Policy*

Experience has shown that commercial policies do not automatically become more liberal when conditions permit them to do so. Direct and determined action is essential to secure the reduction of trade barriers and the promotion of greater equality of treatment; and, as we have argued, it is urgent because this is the time when the whole course of policy is likely to be determined for better or for worse for at least a generation.

When we say it is urgent, we do not mean to imply that quantitative restrictions or other forms of government control over imports can or should be swept away before the maladjustments caused by the war have been corrected and the strains on national balances of payments eased. But the formulation of general objectives of policy and of a general plan for reaching those objectives is a matter of urgency. Among these objectives, our experience from the past has suggested:

(i) the progressive removal, as rapidly as possible, of quantitative restrictions on trade and of exchange control over current transactions;

¹ I approve the better, but follow the worse.

(ii) a substantial lowering of tariffs and the prevention of tariff increases;

(iii) a reduction of administrative barriers to trade;

(iv) a limitation of the use of subsidies affecting international trade;

(v) an adaptation of national financial and economic policies to changes in the pattern of international indebtedness;

(vi) the elimination of trade discriminations through the widest possible application of the m.f.n. clause in its unrestricted and unconditional form;

(vii) the establishment of a satisfactory basis for trading relations between free-market and controlled economies;

(viii) guarantees against discriminatory action by international cartels;

(ix) agreement on a code of principles for inter-governmental commodity agreements;

(x) guarantees of fair and equal treatment of foreigners and foreign firms;

(xi) the establishment of appropriate international machinery, with such powers as may be agreed, to promote the above objectives and in general to facilitate good commercial relations.

A programme of this kind can only be realized through concerted international action; unless concerted action can be arranged to liberalize trade policies it will be difficult for any Government to move independently in the right direction.

3. Proposed Conference on Trade and Employment

During the war years there have been many discussions, some formal and others informal, among various members of the United Nations concerning economic and social questions. The most important declarations arising from these discussions have been clauses 4 and 5 of the Atlantic Charter and Article VII of the Mutual Aid Agreements.

The Atlantic Charter declares:

“FOURTH, they will endeavour, with due respect for their existing obligations, to further the enjoyment by all States, great or small, victor or vanquished, of access, on equal terms, to the trade and to the raw materials of the world which are needed for their economic prosperity;

“FIFTH, they desire to bring about the fullest collaboration between all nations in the economic field with the object of securing, for

all, improved labour standards, economic adjustments and social security.”

This Charter has been adopted by all the United Nations.

In Article VII of the Mutual Aid Agreements the signatory nations are pledged to:

“agreed action . . . , open to participation by all other countries of like mind, directed to the expansion, by appropriate international and domestic measures, of production, employment, and the exchange and consumption of goods, which are the material foundations of the liberty and welfare of all peoples; to the elimination of all forms of discriminatory treatment in international commerce, and to the reduction of tariffs and other trade barriers; and, in general, to the attainment of all the economic objectives set forth in the Joint Declaration, made on the 12th August 1941, by the President of the United States of America and the Prime Minister of the United Kingdom.”

This agreement has been adhered to by over twenty nations.

As we have emphasized in Chapter II, we are strongly of the opinion that the direct association of commercial policies with policies designed to secure an expansion of production and consumption and the maintenance of high and stable levels of employment is an essential prerequisite to progress towards international economic co-operation. The failure in the inter-war years to emphasize the essential interdependence of these issues was indeed one of the reasons for the lack of success that was then experienced. We believe that in present circumstances the most hopeful method of securing progress would be a general conference to deal jointly with commercial policy and the international aspects of employment policy. The United States Secretary of State has stated¹ the intention of his Government to arrange for the convocation of a conference of the principal trading nations of the world within the next year. We trust that if such a conference is convened it will deal with these two related subjects.

If general and comprehensive agreement could be reached at such a conference it would present very obvious advantages. First, the fact that trade barriers were being reduced simultaneously by a large group of countries would facilitate action in each one of them, for each would be able to balance the effect on its domestic industries of the reduction of its own restrictions by the gains for its export industries involved in the reduction of restrictions in other countries. Secondly, as we have emphasized more than once, it is important that, so far as possible, the various aspects of restriction and discrimination should

¹ U.S. Dept. of State *Bulletin*, Vol. XII, No. 302, April 8th, 1945.

be considered together. Thirdly, a speedy re-establishment of "an international framework within which traders and investors in all countries can develop their legitimate activities"¹ is of the utmost importance for reviving economic activity and securing a high level of employment.

We recognize that it may not be easy to secure the immediate adoption of a comprehensive multilateral agreement by every one of the United Nations, and we therefore attach much importance to adequate preparations being undertaken before the conference. We believe that the procedure most likely to secure results might be for a detailed draft agreement, or at any rate a detailed statement of principles, to be approved in advance by as many governments of the United Nations as possible.

In order that the discussions at the conference should not be prejudiced in advance it is naturally important that countries should not raise their tariffs or impose new trade restrictions or denounce existing commercial treaties and agreements before or during the period of the conference. We suggest that a general understanding along these lines should be reached as soon as possible.

4. *International Machinery*

On every subject with which we have dealt in this Report the vital role of adequate international machinery has been made apparent. International machinery is obviously necessary for the preparation of multilateral agreements and of models for use autonomously or in commercial agreements; it is no less obviously necessary in order to plot the course of desired international policies and to bring about a co-ordination of national action through consultation. But it could assist governments in three other ways which have been set out as follows by the Delegation on Economic Depressions:²

"(a) by studying and analyzing the facts concerning the development of trade, the interdependence of different trading areas, the trade in different groups of commodities, the movements in prices, and the changes in the terms of trade;

"(b) by giving advice about means for promoting trade, for clearing blocked channels of trade, about the difficulties arising from sudden changes in production or in the competitive power of different areas, etc.; possibly, in the execution of its advisory functions, participating in trade negotiations between governments in order to watch the

¹ *World Trade and Employment*, Report from the Advisory Committee on Economic Policy to the Committee on International Economic Policy, New York, 1944, page 8.

² *The Transition from War to Peace Economy*, pages 107-108.

effects of proposals submitted during such negotiations on the whole body of trading nations and on the general development of trade;

“(c) by mediating, when so requested, in connection with both direct disputes between states, and on such wider issues as the formation of Customs unions.”

Such international machinery naturally cannot stand alone. It can only function successfully as a part of a system of international co-operation in political and social, no less than in economic, matters. Commercial policy is an integral part of general economic and social policy, which demands a system of economic relationships among peoples designed to ensure stability, prosperity and rising standards of living. Such a system is possible only in a world freed from the threat of war. On the other hand, economic co-operation is of importance not only because of the material benefits it affords but also as an indispensable foundation for a durable system of security. Thus, economic and social progress and political security are essentially interdependent objectives; and on the success of governments in securing their joint attainment depend the prospects of rebuilding a better world.

· ANNEX I

DOCTRINE OF THE ECONOMIC COMMITTEE RELATING TO MOST-FAVOURED-NATION TREATMENT

(Extract from Document E. 805, 1933).

“(a) GRANTING OF MOST-FAVOURED-NATION TREATMENT.

“In fact, different conceptions regarding tariffs and contractual methods appear to be generally associated with different ideas regarding m.f.n. treatment. While the States which refuse to negotiate in tariff matters claim m.f.n. treatment as a preliminary condition of any treaty and as a right which is beyond discussion, on the other hand, those States which have conceived their tariffs with a view to negotiation and who attach more value to tariff agreements than to the juridical guarantee constituted by the m.f.n. clause when it is not accompanied by tariff advantages consider the grant of the m.f.n. clause as subordinate to agreement on tariffs.

“The Committee was of opinion that the Economic Conference of 1927 had not embraced the doctrine which considers equality of treatment as a right above question. It has borne in mind that the resolutions of the Conference declare that each State must judge in what cases and to what extent this fundamental guarantee should be embodied in any particular Treaty. But it has taken care, on the other hand, not to misunderstand that the doctrine clearly affirmed by the Conference was in favour of the reciprocal grant of m.f.n. treatment and in favour of the widest possible extension of its scope and of a liberalism as enlightened as possible in its application.

“In this matter, as in that of tariff and contractual system, the Committee has inclined towards a compromise of fact rather than to a choice between opposing doctrines. It is convinced that, whereas those States which claim m.f.n. treatment by right before any negotiation nevertheless reserve the power to revise it if they run against prohibition duties or unjust discrimination, the States which regard m.f.n. treatment as the price of a favourable tariff agreement nevertheless admit, in general theory, that

this agreement could not be arrived at without the grant of m.f.n. treatment.

"The Committee has noted, therefore, that unanimity could undoubtedly be reached on a doctrine which declared that the grant of m.f.n. treatment ought to be the normal, and that the refusal of this guarantee or the corresponding establishment of a differential regime ought not to arise unless in the case of States which refuse an equitable tariff policy or have recourse to discriminatory practices."

"(b) THE MOST-FAVOURLED-NATION CLAUSE IN CUSTOMS MATTERS.

"The International Economic Conference of 1927 expressed itself in favour of the widest possible application of the most-favoured-nation clause, and recommended:

"(a) That the scope and form of the most-favoured-nation clause should be of the widest and most liberal character, and that it should not be weakened or narrowed either by express provisions or by interpretation;

"(b) The establishment of clearly defined and uniform principles as to the interpretation and scope of the most-favoured-nation clause in regard to Customs duties and other charges.

"The Economic Consultative Committee, at its first session in May 1928, emphasised the importance of having a precise doctrine concerning the interpretation and application of the unconditional most-favoured-nation clause laid down as early as possible, and then confirmed and accepted by an international agreement.

"To give effect to these resolutions, it is essential that the main principles, which are already implicit in the conception of most-favoured-nation treatment, should be stated in the clearest possible terms. We should indeed gain little by inducing countries to use a clause of this description as the foundation of their Customs conventions if the interpretation and consequences of the clause were left open to dispute. It is indeed no exaggeration to say that serious difficulties between countries have sometimes arisen from the different forms and constructions which have been given to this very clause.

"That being so, it is desirable to be very clear as to the scope of this clause in Customs questions, not only so as to arrive at a more exact definition of Customs questions, but also to ascertain

what cases in this field are fit subjects for the application of the clause.

“When the fundamental principles and their field of application have thus been determined, we can proceed to the elaboration of standards for the interpretation and application of the clause, and finally to the drafting of a model clause for the use of Governments in bilateral conventions.

I. Fundamental Principles.

“The most-favoured-nation clause implies the right to demand and the obligation to concede all reductions of duties and taxes and all privileges of every kind accorded to the most favoured nation, no matter whether such reductions and privileges are granted autonomously or in virtue of conventions with third parties.

“Regarded in this way, the clause confers a whole body of advantages, the extent of which actually depends on the extent of the concessions granted to other countries, whether autonomously or in virtue of conventions. At the same time, it constitutes a guarantee, in the sense that it provides completely and, so to speak automatically, for full and entire equality of treatment with the country which is most favoured in the matter in question.

“However, in order that the clause may produce these results, it must be understood to mean that a Government which has granted most-favoured-nation treatment is bound to concede to the other contracting party every advantage which has been granted to any third country, immediately and as a matter of right, without the other party being required to give anything by way of compensation. In other words, the clause must be unconditional.

“As is generally known, conditional most-favoured-nation clauses have in some cases been inserted in treaties, while in other cases existing most-favoured-nation clauses have been construed in a conditional sense, with the effect that a reduction of duties granted to a given country in exchange for a given concession may not be accorded to a third country, except in exchange for the like or equivalent concessions. This opinion is based on the conception that a country which has not, in some given respect, made the same concessions as another is not en-

titled to obtain, in this respect, the same advantages, even if it has made wider concessions in other respects. It cannot, however, be too often repeated that a conditional clause of this kind—in justification of which it is argued that, if it does not grant equality of tariffs, it offers at any rate equality of opportunity—has nothing whatever in common with the sort of clause which the International Economic Conference and the Economic Consultative Committee recommended for the widest possible adoption.

“It is in fact the negation of such a clause, for the very essence of the most-favoured-nation clause lies in its exclusion of every sort of discrimination, whereas the conditional clause constitutes, by its very nature, a method of discrimination; it does not offer any of the advantages of the most-favoured-nation clause proper, which seeks to eliminate economic conflicts, to simplify international trade and to establish it on firmer foundations. Moreover, it is open to the very grave objection of being unfair to countries which have very few, or very low, duties, and which are thus less favourably situated for negotiating than those which possess heavy or numerous duties. The arguments in support of a conditional most-favoured-nation clause tend in reality to favour the maintenance of high tariffs, and place countries which have low tariffs in a position of inferiority; the result must be to create or foster tendencies in direct opposition to the recommendations of the Economic Conference. This does not mean, as will be shown below, that certain exceptions of a general character to the rule of most-favoured-nation treatment cannot be admitted—provided that there are special circumstances to justify them.

“We may therefore conclude that the first fundamental, principle, implicit in the conception of most-favoured-nation treatment, is that this treatment must be *unconditional*.

* * *

“Moreover, in order to allow for the free play of competition in international trade and to prevent the reintroduction of discrimination, the clause needs to be, not only unconditional, but also unrestricted; in other words, it must apply to the whole of the tariffs of the contracting countries.

“If the clause is made not to apply to a large number of articles or even to a single article which plays an important part in the trade between two countries, it ceases to provide equality

of treatment with any third State and, on the contrary, results in actual discrimination as between the country which is thus excluded from certain advantages in respect of particular goods and the country or countries which receive such advantages.

“Such discrimination may, in a certain sense, be regarded as legitimate, if it has been agreed to by the country which it affects. But this in no way avoids the restrictive effect which such a practice produces, not only on trade between the contracting parties, but also on the normal development of international trade.

“Moreover, the discrimination which is implicit in the restricted clause can manifestly produce no other effect than to afford special protection to internal producers against the competition of certain producing countries, or to grant certain foreign countries a preferential position.

“In either case, such a restriction could only be accepted with reluctance, and consequently an agreement based on the restricted clause could merely be regarded by the contracting party who is the chief sufferer by the restrictions as a lesser evil than the absence of any agreement whatsoever in regulation of trade.

“No doubt it may sometimes happen that these restrictions affect both parties to the same extent; but in such a case the agreement based on the granting of limited, though ostensibly equivalent, advantages only constitutes a very imperfect application of the most-favoured-nation treatment.

“In view of the above considerations, we may conclude that the clause must be, not only unconditional, but also *unrestricted*; in other words, that it must apply to all the goods which two countries exchange or may exchange with one another.

* * *

“If the clause fulfils these two fundamental conditions—in other words, if it is unconditional and unrestricted—it assures the best treatment which two countries can possibly grant one another in Customs questions.

“In other fields, the most-favoured-nation clause, even if unconditional and unrestricted, only represents on the contrary a minimum of the privileges and safeguards which two countries can grant one another; we would instance as examples: the treatment of nationals permitted to engage in business in a foreign country (the right of establishment), the payment of direct and indirect taxes on the exercise of any commercial ac-

tivity, the payment of internal taxes on the manufacture, distribution and consumption of goods, and also on navigation (not including coastal traffic).

“Without going further into these questions, we may observe that it is generally admitted—either in theory or in international practice—that, in regard to the points we have just mentioned, national treatment is as a rule an indispensable condition for the free and productive growth of co-operation between peoples; in consequence, the most-favoured-nation clause can in such cases only offer an additional safeguard supplementing those already provided by national treatment.

“On the other hand, it must be admitted that, in regard to certain questions, the treatment provided by the clause is too wide in its scope and that these questions can only be properly regulated on a reciprocal basis. This applies, for example, to double taxation.

“But in Customs questions, it must be repeated, the clause represents the maximum of advantages and safeguards, and must be recommended as the fundamental stipulation on which international commercial relations should be based—provided always that it fulfils the two above-mentioned pre-requisites, *i.e.*, that it is unconditional and unrestricted.

“It will be seen that the Economic Conference had sound reasons, in the resolutions quoted at the beginning of this report, for restricting the study of the problem to Customs questions.

II. *Field of Application.*

“What is to be understood by Customs questions for our present purposes?

“According to the general practice in commercial treaties, the term ‘Customs questions’ includes the scales of Customs duties and the method of levying them—*i.e.*, import and export duties supercharge co-efficients, where they exist, and subsidiary charges of every sort levied on imports or exports. The term also covers all the rules, formalities and charges inseparable from Customs operations of every description (including, for instance, the regulations for the treatment of passengers’ luggage or commercial travellers’ samples; the procedure and time limits for appeals to administrative, judicial or arbitral authorities against Customs decisions relating to the application of tariffs).

“There are, however, two highly controversial questions which it is necessary to consider; namely, whether the clause applies to import or export prohibitions, and whether it applies to temporary imports and exports, including finishing trade.

(1) Import and Export Prohibitions.

“As regards import and export prohibitions, that question is governed in many treaties by the most-favoured-nation clause, whereas in others prohibitions are regulated by special clauses in which the contracting parties undertake only to enforce them in the recognised exceptional cases (reasons of health, public safety, protection of Government monopolies, etc.) or in cases of extraordinary economic necessity that might arise, with a view to protecting the vital interests of the country.

“As you are aware, the principle universally recognised prior to the war was that of freedom of trade; in other words, prohibitions on economic grounds were non-existent. There was therefore no occasion to demand the most-favoured-nation clause in questions of this sort.

“The war made it necessary to close the markets wholly or in part to a number of articles, indeed in some cases to goods of all kinds. The abnormal economic situation in the period immediately after the peace induced many Governments to make considerable use of prohibitions. During this period (and in this connection), the application of most-favoured-nation treatment was frequently refused, and any exceptions granted were solely on a basis of strict reciprocity—in most cases in virtue of special so-called countervailing agreements, and within the limits of specified quotas, what might perhaps be called a mixed system was adopted in some countries: in cases where all or most of the prohibitions had already been abolished in trade with a given country, the same concession was extended to other countries who could show that they did not make use of prohibitions themselves and who demanded their abolition in virtue of most-favoured-nation clauses in treaties in force between the parties.

“As the situation gradually became more normal again, the principle of most-favoured-nation treatment gained ground and was expressly stipulated in a number of treaties, some of which also provided that such concessions should be limited to quotas.

“One question continued to be a subject of keen debate: whether, in cases where the most-favoured-nation clause was not

expressly extended to the import and export system, regarded in the above sense, prohibitions should nevertheless be deemed to come under the clause, as falling within the general boundaries of Customs questions; or whether, on the contrary, they should be governed by the principle of reciprocity?

“It must be admitted that the extent to which a Government is able to concede exceptions in the matter of prohibitions to another country is dependent, not only on the system in force in that country, but also on the relative situation and importance of industry and markets. If the clause is held to apply narrowly in such matters, this might be held to involve an obligation to extend facilities which have been granted to a given country in view of certain conditions peculiar to that country to other countries where the same conditions do not obtain. Such a result would, in a sense, be in conflict with the very principle of equality underlying the clause.

“Moreover, if a country is to allow all countries admitted to most-favoured-nation treatment the same quota which it feels able to concede to a given country, the prohibitions would in practice cease to have any effect.

“For these reasons, we should, in principle, conclude that the standard most-favoured-nation clause herein suggested does not, unless otherwise expressly stipulated in commercial treaties, apply to prohibitions. But we must not forget that this solution does not entirely meet the present situation. Although prohibitions have in the main been abolished, some still exist, and, as long as this continues to be the case, it would be desirable that the interpretation adopted during and after the war, to the effect that the clause should apply as far as possible to prohibitions, should still be adhered to.

“Fortunately, the Geneva Convention of November 8th, 1927, has reaffirmed the principle of freedom of trade in regard to imports and exports. When that Convention has come into force, the questions we have just been discussing will have lost much of their practical interest.

“It may be appropriately pointed out, in this connection, that the Protocol of that Convention contains a declaration to the effect that an equitable allocation of quotas is one of the essential conditions of the equitable treatment of international commerce.

(2) *Customs Quotas.—The Various Classes of Quota.—Ways in which they are applied.—Are they compatible with the Unconditional and Unrestricted Most-favoured-nation Clause?*

“When we consider the various cases of Customs quotas established by the general (autonomous) tariffs of certain countries or fixed by bilateral agreements, we are bound to admit that there is no common measure applicable to them all, and that, according to their economic importance and their object, they must be divided into four classes.

“(a) Certain Customs quotas have no other object than to regulate the traffic in certain goods between neighbouring zones in adjacent countries. This is not frontier traffic in the strict sense, because the range of 10 or 15 kilometres is greatly exceeded; nor, on the other hand, is it a traffic that concerns the entire territory of the two adjacent States. Still less is it likely to be of any interest to third countries. It is perfectly clear therefore that these quotas have not been established with the object of limiting the possible imports of third countries benefiting by the most-favoured-nation clause, and it would not appear that the question whether they are compatible with the clause can arise.

“The cases which might be placed in this class are fairly numerous. Some of them seem to bear a very close resemblance to frontier traffic (*e.g.*, the quotas established in the commercial treaty between Austria and Switzerland of January 6th, 1926); others are subject to conditions such as to limit the traffic in the goods in question to certain parts of the territory, whereas, if no such conditions existed, the local traffic would probably develop into a much more extensive traffic (*e.g.*, the quota for *mirabelles* and strawberries in the commercial agreement between Belgium and France of February 23rd, 1926).

“(b) Other quotas are designed to limit the importation of a commodity which the importing country does not produce, in order to make it more difficult for that commodity to compete with similar goods manufactured in the importing country. In the case of these quotas, there is no idea of restricting imports of the commodity in question from third countries, seeing that it is a special product of one particular country and is not, generally speaking, produced in any other country.

“We may say, indeed, that since the quota in question has the effect of making it more difficult for the commodity in ques-

tion to compete with similar goods produced in the importing country or in *other* countries, it may be beneficial to the latter.

“Such is the case of the Customs quota established in the Italo-German Treaty of October 31st, 1925, for maraschino spirit, and in other treaties concluded by Italy in respect of maraschino.

“Seeing that other countries do not produce that liqueur but do supply the importing country with other liqueurs, it seems clear that the quota in question may be more to their advantage than to their detriment, and so the question of the compatibility of the quota with the clause cannot arise.

“(c) From these two classes of quota, which are of very little importance in international trade, and which do not seem likely to give rise to any dispute, we pass to a third class—that of quotas established rather to *regulate* than to limit the importation of a given commodity.

“It may chance that the industry in the importing country is passing through a period of temporary difficulties and might be destroyed or seriously prejudiced by excessive imports.

“On the other hand, it may also chance that the commodity in question is a raw material for another industry in the same country, so that its importation cannot be limited without favouring one industry at the expense of another.

“The result of this situation has been the establishment with the various importing countries—not with only one of them—of Customs quotas proportionate to the importing capacities of the different countries and corresponding in their aggregate to the normal aggregate imports.

“Such is the case of the quotas established by Germany for imports of cotton yarns, in the treaties she concluded after the war with various European countries.

“In this case, we have not a single quota established with one particular country and applied to others equally or proportionately on the basis of the most-favoured-nation clause, but several quotas established with the various countries concerned, which, by accepting them, implicitly admit that they answer to their needs.

“If, now, there is a country which is also interested in the importation of the commodity in question but with which no quota has been established, that country will undoubtedly be entitled to demand that the same be done in its case, unless it is content to require, on the basis of the clause, the application of the

highest quota or of a proportionate quota, according to whether the system of equal quotas or that of proportionate quotas has been adopted.

“This third class of quota is undoubtedly of importance in international trade; but as such quotas are generally designed to *regulate* rather than to limit imports, and as the various quotas are established in agreement with the principal countries affected, there seems no reason why disputes should arise.

“(d) The case is quite different when a Customs quota is established in a commercial agreement between two countries and is then applied equally or proportionately to other countries in virtue of the clause.

“If, as frequently happens, the quota is established with the country least interested in the exportation of the commodity in question, and if, as is also often the case, the Customs duty on additional quantities is too high, the inevitable result is that the aggregate imports are restricted at the expense of all the exporting countries, except possibly the country with which the quota was originally arranged; and this restriction is prejudicial to the various countries concerned in direct proportion to their exporting capacity.

“Whereas with freedom of importation every country has a right to import enough goods to meet its demand, the quota upsets this situation, and transforms that right into the right to import a fixed quantity of goods (equal quota) or a quantity of goods proportionate to that which each country would be entitled to import (proportionate quota).

“Whereas the most-favoured-nation clause places all countries on the same footing—which is to say, on equal terms in international commercial competition—the quota upsets this situation by applying a common measure to all countries, irrespective of their output and their competitive strength.

“This fourth class includes certain quotas recently established; and it is in connection with these quotas that the question of compatibility with the most-favoured-nation clause arises.

“The quotas we have attempted to divide into a number of main classes according to their object lend themselves to numerous distinctions according to the ways in which they are applied.

“Quotas can be distinguished according to the period for which they are established; according to whether they are explicitly or tacitly renewable; according to the conditions imposed on the

importation of the quota quantities; according to the Customs treatment they receive, and so forth.

“These details do not alter the legal character of the quotas, and do not seem to have any influence on the question of their compatibility with the clause.

“On the other hand, they are of great practical importance, because they show that Customs quotas are always a hindrance to trade, varying in its gravity according to the nature of the conditions laid down for the importation of the quota quantities (*e.g.*, the obligation to import through certain specified Customs houses or within a specified time, and the like). Indeed, the conditions are sometimes so difficult to fulfil, especially for certain countries, that there seems some reason to ask whether—quite apart from the fact that they encroach upon the rights conferred by the most-favoured-nation clause—they do not offer the characteristics of an actual indirect protectionism, amounting to an intrinsically unjustifiable discrimination.

“We shall not therefore dwell upon the methods of application, which, generally speaking, do not seem very important to the solution of the question; but we do think it necessary to call attention to the difference in the character of Customs quotas according as they are established by a bilateral commercial agreement or by an alteration introduced in the general tariff of a country by an autonomous act:

“If the quota is established by a bilateral tariff agreement and is subsequently applied to third countries in virtue of the clause, then the question does arise.

“If, on the other hand, it is established autonomously by an alteration in the tariff, it is open to doubt whether the question does or does not arise, and in what case.

“If the quota is established as an aggregate, all countries may share in it according to their competitive strength. The condition of equality guaranteed by the clause is not infringed. The aggregate quota may injure the position of all third countries, but it would not constitute a breach of the most-favoured-nation clause.

“The loss inflicted on exporting countries arises in this case from the limitation of imports which is a feature of the aggregate quota. But if the country which has fixed such a quota had the right to restrict the importation of the goods under con-

sideration, it seems that there can be no question of any breach of the rights of third States.

“It should, however, be noted that instances of aggregate quotas are extremely rare, on account of the difficulties to which they give rise. For all exporting countries will endeavour to arrive first in the race for importation. Consequently, if at the moment the aggregate quota comes into force there happens to be already at the frontier a quantity of goods—of varying countries of origin—greater than the aggregate quota, the country which has fixed the quota will be obliged to admit the whole quantity (which may be contrary to its own interests), or it will have to establish some allotment among the various exporting countries; in which case the quota will cease to be an aggregate quota.

“But if, instead, the quota fixed by an autonomous act is established to allow equal quantities for all countries or quantities proportionate to their exporting capacity, then the question arises of the compatibility of equal or proportionate quotas with the clause.

“Actually, the most-favoured-nation clause gives the right to share in all concessions made, not only by commercial treaty, but also by autonomous act.

“Consequently, any conclusion arrived at with respect to the compatibility with the clause of quotas fixed by commercial treaty is equally valid for quotas fixed by autonomous act.

“It should, moreover, be noticed from a practical standpoint that, if Customs quotas fixed by autonomous act were not governed by the most-favoured-nation clause, any country wishing to avoid obligations arising out of the clause would merely have to avoid fixing a quota by commercial treaty.

“Thus, if we admitted that Customs quotas fixed by autonomous act were not governed by the most-favoured-nation clause, it would be equivalent to admitting that a country having by commercial treaty granted some specific Customs concession and received its equivalent might arbitrarily limit this, even to the point of rendering it illusory, by fixing by autonomous act an equal or proportional quota, as a consequence of which the exporting capacity of the contracting country might be reduced or even disappear entirely.

* * *

“After these considerations, the primary object of which was to define the true scope of the problem, we can now consider

the question of the compatibility of Customs quotas with the clause.

“In the first place, it should be pointed out that the most-favoured-nation clause has two objects: (a) to secure to the country enjoying its benefits a total of advantages represented by all the Customs concessions and privileges granted to third countries and by all the concessions made by autonomous act, and (b) to ensure absolute equality of treatment by guaranteeing to all countries which enjoy its benefits equal terms in all matters covered by commercial treaties and, as a result, the free development of their economic aspects.

“The total advantages assured by the clause are not fixed or immutable. They may be increased if the State that grants the most-favoured-nation treatment concludes new commercial treaties making new or greater concessions in favour of other States or grants fresh privileges or advantages by autonomous act. They may decrease if one of the former commercial agreements becomes null and void, or if one of the privileges granted by autonomous act is withdrawn. For that reason, a State which in virtue of the clause has had the right to import an unlimited amount of certain goods at a given Customs duty cannot claim that the clause has been violated merely because the duty in question has been raised later by means of an autonomous provision and it only continues to benefit from the former duty for quantities corresponding to a Customs quota.

“But, if a State is not entitled to preserve unchanged the original advantages of the clause, it certainly has the right of insisting that the principle of equality of treatment which is assured by the clause, and which consists in guaranteeing every country equal conditions where international commercial competition is concerned, should not be departed from.

“If the question is considered from this point of view, it is clear that Customs quotas might be contrary to the clause, if they mean that all countries shall be granted the right to import an *equal* quantity of goods at a favoured tariff. A country is not an abstract entity, but a concrete reality. The constituent elements of this reality are a country's population, territory, state of civilisation, agricultural and industrial development, geographical situation, etc. Each country differs from other countries in so far as it has more or less of each of these elements or of their sum; and each country asserts itself before other countries as a

concrete entity which strives to develop its powers and resources to a maximum.

“The most-favoured-nation clause cannot therefore ignore the facts and attempt to destroy the special commercial position of a State in relation to other States.

“On the contrary, the object of the clause is to preserve these respective positions intact, by treating all countries *on the same footing*, which is quite a different thing from treating all countries in a mechanically equal way. While the clause does not prevent the country granting it from taking all measures which depend on its own sovereignty, even if these render the treatment originally granted less favourable, it certainly forbids the adoption of any provision likely to modify the situation of a State in relation to the other States in so far as commercial competition in a given market is concerned.

“Now, if Customs quotas are applied in such a way as to give all States, whatever their power of competition, the right to import an equal quantity of goods at a reduced duty, all countries would be brought to the same level, and the relation of one country to another might be seriously upset. If this disturbance of equality in international competition is to be avoided, we must, as a general rule, either give up the idea of equal quotas or at least fix them in such a way as not to injure third countries.

“Our conclusion concerning *equal* quotas cannot be applied in identical terms to proportional quotas.

“If, in fixing proportional quotas, account could be taken of the respective powers of competition of the various States, so as not to vary in the least degree the relations of a State to other States so far as commercial competition in a given market is concerned, then such quotas should be recognised as in keeping with the most-favoured-nation treatment.

“But this is purely theoretical. In practice, it is found impossible for a country to fix proportional quotas so as not to interfere with the free play of international commerce.

“On what basis is the exporting capacity of individual countries to be decided? Statistics of international trade can only provide an approximate figure, seeing not merely that production, particularly in agriculture, may vary considerably from year to year, but particularly that the trend of trade is continually changing and that a shrinkage in any given market arising from a natural fall in demand or from some artificial hin-

drance (high tariffs, import prohibitions, etc.) has, as its natural consequence, a reflux of larger quantities of goods to other markets.

“On the other hand, if proportional quotas were established so as to maintain intact the exporting capacity of every country, then these quotas would hardly fulfil their purpose, which is always to *regulate* importation, more or less artificially, and frequently to *limit* it.

“Actually, in practice, we see that a proportional quota is sometimes fixed in the first instance for a country which, having only a very slight interest in the export of the product in question and perhaps finding compensation elsewhere, is quite prepared to accept a relatively low percentage. The same percentage is then applied to those other countries which enjoy most-favoured-nation treatment. The result is that all, especially those countries more particularly interested, find their interest severely prejudiced, sometimes to an even greater degree than would have been the case if the quotas had been fixed at an equal quantity for all, allowing some latitude.

“Moreover, proportional quotas are very rare in practice.

“In fact, except in the above-mentioned case of veritable collusion between two States to the detriment of a third, it is difficult for a State to be content with a low percentage; and, in that case, the Customs quota cannot succeed in its aim of reducing the normal exports of all States to an appreciable degree.

“On the other hand, *equal* quotas may be fixed on the basis of the *total* exports of a given country, which will doubtless find no difficulty in consenting to that. If the same quota is then applied to other States, the desired result will be easily and surely attained.

“Consequently, it seems possible to conclude that proportional quotas are less dangerous than equal quotas, because it is more difficult to fix them in such a way as seriously to disturb the existing position.

“But even these quotas are an obstacle to commerce, and may give rise to arrangements that seriously prejudice the interests of third States.

“They are therefore not to be recommended, and it would even be best, in the higher interests of commerce, to avoid them carefully.

“From the foregoing considerations it might appear that Customs quotas, whether equal or proportional, are all to be condemned, although in varying degrees.

“However, to come to such a conclusion would perhaps be excessive. It would ignore the arguments of irrefutable value, used by those who support the system of quotas—namely, that quotas are frequently used as a weapon of moderation in Customs warfare, and as a means of conciliating the opposed interests of national producers and importing States.

“It is argued that, if it were impossible to have recourse to Customs quotas, the increase of duties would cover the total quantity of goods imported, and in the case of a large increase the harm suffered by exporting countries would be much more serious.

“This consideration is true, but its importance should not be exaggerated.

“First, if the increase of duties were to cover all imports, it would raise such opposition and protests from those inside the country who were hit by it, that there would certainly be a strong tendency towards greater Customs moderation. On the other hand, Customs quotas make it possible to conciliate divergent interests at home, and thereby make it easier to raise duties.

“Secondly, it is doubtful whether the system of Customs quotas is better for exporting countries than the system of unlimited exports for all countries at equal, although high, rates. If we put ourselves in the position of a country whose exporters have spent enormous sums on advertisement and commercial organisation in order to obtain a particular market, and who may find themselves at any moment compelled by a Customs quota to export so limited a quantity of goods that they would have to look on all their past expenses as lost, and find it impossible to support the cost of maintaining the organisation they have built up, all of which would be to the advantage of their competitors, who would thereafter have the same position in the market as themselves, it may well be wondered whether these exporters would not prefer a higher duty, instead of any quota.

“The argument is a fair one, but it goes too far, for it is not true that Customs quotas improve the position in every case; on the contrary, they often make the position more intolerable.

“It may be said, in general, that Customs quotas can be con-

sidered not harmful when their purpose is, not to upset the positions exporting States have obtained in a certain market, but to systematise and regulate them. There are Customs quotas which have helped to settle notable difficulties without prejudice to third States.

"This is the case, for example, with the cotton yarn quota agreed upon by Germany with the principal exporting countries, with the wine quota conceded by Austria to Italy, and with the cement quota conceded by Italy to Austria.

"Such examples could be multiplied. No complaint has ever been raised against quotas of this kind, because they were devised in such a way that they did not harm the interests of third parties.

"It would therefore be unjust to condemn quotas without distinction by renouncing the advantages they sometimes offer.

"The regulation of commercial relations between States so bristles with difficulties because of unbridled protectionism that no means of arriving at a satisfactory conciliation of the diverging interests without harming the rights of third parties should be neglected.

"But how can the rights of third parties be safeguarded in agreements in which they cannot participate and the consequences of which are automatically extended to them by reason of the most-favoured-nation clause?

"It appears that the best solution is to decide that quotas should be fixed by agreement with the country which occupies the first rank among the countries importing the goods in question.

"In this case, the quota is fixed by agreement with the country whose interest it is to obtain the largest amount. It is hardly probable that such a quota should totally, or in a great part, satisfy countries which have smaller exports.

"Certainly, there may be drawbacks and abuses even in this procedure. For example, it may happen that the country whose exports are the highest may be unable for various unforeseen reasons to assert its interests with the necessary energy and may content itself with a quota insufficient for the needs of a country whose exports are smaller than its own.

"But those are exceptional cases which should not distract us from the main issue. A country which exports the greatest quantity of a given merchandise ought ordinarily to be defending

so vital an interest that it is in a position to put up a much stronger resistance than the other parties concerned.

“However that may be, the most important thing to be noted is that, if the Customs quota is agreed upon with the country most directly interested, there is less risk of displacement of commercial positions, which is the real weak point of quotas, and the main reason why they are incompatible with the most-favoured-nation clause.

“As a conclusion it may be stated that Customs quotas, which are a consequence of excessive protectionism, nearly always tend to increase this protectionism.

“Not content with having put up a first barrier by means of high tariffs, countries erect a second by fixing quotas so as to limit imports to an even greater extent than was possible by high tariffs.

“And in order to make more certain of achieving their object, they endeavour particularly to hinder exportation from those countries which have the greatest penetrative power.

“Thus, it is inevitable that quotas should disturb the freedom of competition between the various countries interested, so that they develop into a violation of the most-favoured-nation clause.

“As a general rule, therefore, they are to be condemned and avoided.

“If, however, their tendency is to *regulate* the import trade by helping to tide over periods of temporary difficulty, in such cases they must be so fixed as to cause a minimum of injury to the interests of third countries.

“Any country desiring to adopt Customs quotas must bear in mind that the most-favoured-nation treatment which it has conceded to other countries imposes on it the obligation not to impair the equality of conditions in international commercial competition; therefore, quotas must be fixed so as to safeguard, as far as possible, the position of the countries interested. Whether this is done by fixing the first Customs quota with the principal exporting country, or by negotiations conducted with each of the various interested countries in turn, is not a matter of essential importance.

“What is of importance is that the interests of the various countries enjoying most-favoured-nation treatment should be considered and respected.

“It is only in this way that Customs quotas, the expedient of

a period of excessive protectionism, can be regarded as admissible and, at the same time, attain the desired end without aggravating a situation already far from satisfactory.

(3) *Temporary Imports and Exports.*

“As regards the second question we mentioned, a distinction must be drawn between temporary imports and exports in the true sense of the term and the so-called finishing trade.

“In regard to the former, the clause applies to all concessions which, being solely designed to facilitate international trade, relate only to goods which are not intended to undergo any further transformation (for instance, containers, imported empty and re-exported full, implements and apparatus intended for the erection of plant and re-exported on completion of the work; goods sent to fairs or exhibitions and re-exported because they have not been sold).

“On the other hand, the special cases of temporary imports and exports which come under the description of finishing trade give rise to the following considerations:

“A distinction must be drawn between ‘active’ finishing trade and ‘passive’ finishing trade.

“The term ‘*active finishing trade*’ is employed when a Government authorises the importation free of duty, or at a reduced rate, of foreign goods (usually raw materials or semi-finished articles) on condition that such goods are transformed into finished articles of a specified character intended solely for export.

“‘Active’ finishing trade is authorised solely in the interests of the importing country. The latter permits the goods to enter duty-free to the extent that it desires to place raw materials or half-wrought articles, which its manufacturers require in order to make finished products for export, at the disposal of its industries at lower prices than those obtaining in the home market. The loss in revenue represented by the exemption from duty is offset by the economic gain resulting from increased sales abroad. For these reasons, the measures under which such exemption is granted are of an autonomous character and are scarcely ever the subject of negotiations or conventions with foreign countries; the latter cannot, indeed, fail to benefit by measures exempting goods which would otherwise be dutiable. There is therefore no clash of interests and consequently no ground whatever for discussions or negotiations.

“Nevertheless, although the measures relating to temporary imports (‘active’ finishing trade) are, by their very nature, solely dependent on the will of the country applying them, it would be impossible to understand or to defend a restriction under which goods imported from particular countries would alone be admitted free of duty.

“The importing country seeks in one way or another to attain a certain result, which is solely in its own interest, no matter from what foreign country the goods may be imported.

“Consequently, a measure restricting the exemption to goods coming from particular countries could only be designed to establish an unfair discrimination at the expense of the countries debarred from this privilege. Any such restriction must therefore be condemned.

“Moreover, it would be in flagrant contradiction with the principle of equality of treatment, implicit in the most-favoured-nation clause, if a country to which this treatment had been granted in Customs questions were to be debarred from the privilege of exemption.

“The most-favoured-nation clause must therefore be applicable to ‘active’ finishing trade, it being understood, however, that, when the laws of a country make this trade dependent on an administrative decision, the right of the competent authorities to take a decision in each particular case is in no way affected thereby.

“The Economic Committee arrived at a somewhat different conclusion in regard to *‘passive’ finishing trade*.

“‘Passive’ finishing trade arises when a country authorises the temporary export of certain goods, and readmits them free of duty when they return to the country after being finished abroad.

“The goods concerned in ‘passive’ finishing trade are, as a rule, articles already partly finished, or almost completely finished, which merely have to undergo a final process (as, for example, fabrics which have to be dyed, embroidered, etc.). This trade cannot therefore take place without the consent of two parties: the exporting State, which promises to readmit the finished article free of duty, and the importing State, which offers exemption from duty for the article when it is brought in to be finished.

“The consent of these two parties may find expression in two different and autonomous sets of measures, each of which is com-

plementary to the other; or it may be embodied in a bilateral agreement in which the intentions of both sides are harmonised and defined for the better realisation of their common object.

“But, in whichever of these two forms the consent of the parties finds expression, the fact remains that ‘passive’ finishing trade is usually to be accounted for by the special situation which the producing industry of one country occupies in relation to the finishing industry of another country.

“Consequently, the origin of the few existing cases of ‘passive’ finishing trade and the reason for their continued occurrence must be sought in the special economic, industrial and historical relationships between certain countries.

“Nevertheless, among the countries which follow an autonomous policy in regard to temporary exports, a certain number apply the most-favoured-nation clause to the ‘passive’ finishing trade. These countries, it is true, reserve the right to decide, independently and of their own free will, whether or not they will allow temporary exports, but having made their decision they will allow goods to be exported in this way to any of the countries entitled to most-favoured-nation treatment.

“Other countries, on the contrary, deny that ‘passive’ finishing trade can be governed by the most-favoured-nation clause, arguing that a concession which could be defended in regard to one country might have no justification in regard to another.

“Having regard to the diversity of opinions and systems, the Economic Committee did not feel able to advocate the application of most-favoured-nation treatment to ‘passive’ finishing trade. It did, however, express the opinion that a country would only be justified in refusing, under the most-favoured-nation clause, to extend to others the concessions already granted to one country, if the other country demanding them were quite differently situated—in regard to the circumstances in view of which the concessions were allowed—from the country to which they had originally been granted.

“It follows that the discrimination must be founded on objective considerations and not on arbitrary views or preferential tendencies. In the absence of such justification, discrimination could not be regarded as compatible with the attitude which countries must observe in their dealings with one another if they wish to maintain normal and friendly relations.

III. *Essential Characteristics of Goods benefiting by the Clause.*

"After determining the scope of application of the clause, one must be clear as to the conditions which goods must fulfil to qualify for most-favoured-nation treatment.

"The two essential conditions are as follows:

"The goods must *have their origin* in the country which enjoys most-favoured-nation treatment, and they must be *like products*, in the sense that they must possess the characteristics which entitle certain goods to a given Customs treatment.

"(1) According to the systems adopted in different countries, most-favoured-nation treatment is granted, either to goods in provenance from the country which claims the benefit of the clause or to goods originating in that country, or again to goods which both originate in and are in provenance from the country entitled to most-favoured-nation treatment.

"The rule of provenance, as a sole condition, may be disregarded, not only because it is so rarely used, but also because it is designed to favour direct traffic between the contracting countries and hence to discourage the despatch of goods through a third State—thereby deflecting the trade from its natural channels. The rule of origin, on the other hand, must be regarded as an essential condition, since the aim of commercial treaties is to encourage the contracting parties to exchange their respective native products.

"The rule of provenance may, however, be regarded as a supplementary factor in cases where additional safeguards have to be sought, when, owing to special circumstances, a differential regime is in force in regard to one or more countries.

"But, having noted that the essential condition must be the origin of the goods, we have still to ascertain, in the interests of precision, when an article has its origin in a given country. This problem—which is simply that of the nationality of the goods—is easy to solve in the case of *natural* products—*i.e.*, of products of the soil and of the sub-soil. All States are in agreement in regarding as the country of origin of these products the country in which they have been *harvested*, or *obtained* in any other way. On the other hand, the problem becomes one of the most complicated and difficult points in commercial policy owing to the increasing complexity of industrial production and of the constantly closer international co-operation which results therefrom when we come to deal with *manufactured* products.

“For though a certain number of articles are made from native raw materials of a single country and have been through all the processes of manufacture in that country, there are others which contain a greater or less proportion of raw materials originating in other countries, or on which in varying degrees work has been expended in other countries, and we find even extreme cases of articles which have only undergone the last finishing process in the country in question. It is very difficult to determine at what point the manufacturing process performed in other countries must prevail over the work done on the article in the country itself. The problem is further complicated by the diversity of systems and standards adopted in this respect by the different legislations. In some States, the country of origin of a manufactured product is that in which it has been *worked up* or *manufactured*; in others, that in which the product has been manufactured or transformed, with the proviso, however, that the value of home raw materials and home labour must represent *a given percentage of its total value* (sometimes 25 and sometimes 50 up to 75 per cent). Other States confine themselves to requiring that the manufactured product should contain a *considerable* proportion of home labour, or that the product should have undergone in the country an *important transformation*, or its *last industrial transformation*, or that the *finishing* should have been done by home labour, etc. In addition, some States have laid down that the raw or semi-manufactured materials which have been worked up or manufactured in the country in question must have paid import duty, whereas other countries allow that the work should be done on goods introduced under the system of temporary importation.

“The system of percentual increases in the value, which may appear theoretically sound, breaks down altogether in practice in face of the great difficulty for the importers of furnishing workable evidence of the increase of value, and the virtual impossibility for the Customs of obtaining positive information on the point. Moreover, past experience in regard to this formula is sufficient to show its extremely unreliable character.

“On the other hand, a formula such as *the country of origin of manufactured products shall be taken to be the country in which such products have undergone important transformation* would seem at first sight satisfactory. But some definition of the term *important transformation* should be given. An exact and

precise definition of this term of a nature to rule out any arbitrary action on the part of the Customs administration is, however, impossible. It is possible, for example, to treat as important any finishing process the consequence of which is to bring a product in the country of definition under a different tariff specification from that which would otherwise have been applicable to it, or—following up the same idea—any finishing process the consequence of which is to make the product liable to higher tariff rates than those to which it would otherwise have been subject. This criterion might, however, prove inadequate in practice on account of the differences of tariff specifications in different countries, as a result of which the effect of the formula would not be the same in all countries.

“If, leaving on one side the question of a formal definition of *important transformation*, it was desired to follow the method of giving an idea of what was to be meant by this expression by quoting as examples some of the operations which should be regarded as important, or *vice versa* some of the operations which should not be regarded as important, other difficulties would be encountered. Lists of this kind, which would necessarily be illustrative and not exhaustive, and would consequently be very incomplete, would raise a great many doubts, and would indeed obscure the question instead of clearing it up.

“In conclusion, and setting out from the fact that treaty provisions have sufficiently brought into line the divergent standards adopted in the different countries, and from the axiom that in the interests of international trade the problem should be settled in a liberal spirit, it seems advisable to adopt the following principles:

“The basis taken for the purpose of determining the nationality of a product shall be its origin. The origin declared at the Customs shall be accepted, provided that such evidence of origin or consignments as the legislation of the importing country may require is produced, and provided that there is no presumption of the incorrectness of the declaration of origin.

“The country of origin in the case of *natural* products shall be taken to be the country in which such products have been grown, harvested, extracted or in any other manner obtained, or, in other words, the products of the soil or sub-soil of the country in question.

“The country of origin of *manufactured* products shall be

taken to be the country in which such products have been finished. No account shall be taken of the origin of the raw materials or of the raw, semi-manufactured or manufactured products which have entered into the composition of a product, or of the fact that the work of manufacturing or finishing took place in free circulation or under Customs supervision, except, however, in the case in which finishing is only aimed at evading payment of a higher duty.

“This reservation in regard to operations which are carried out with no other object than to evade higher duties applicable to the products if imported direct from the country of origin is a necessary precaution if the Customs are not to be left defenceless in the presence of fraudulent proceedings.

“After laying down the conditions of origin of goods, it seems necessary to consider the conditions in which the goods must be consigned and transported in order to retain their origin. Although the great majority of States accept the principle that goods retain the origin of the country of production or manufacture even if they reach the country of destination after having gone through other countries, remained in warehouses and undergone therein the handling necessary for their preservation or a change in their packing, there are, none the less, countries which require that goods should reach them *direct* (*en droiture*) in order to be entitled to preferential duties, this term, ‘*en droiture*’, being interpreted in a more or less wide sense.

“But here, too, commercial treaties have brought the different conceptions closer together, and the most liberal doctrine has become increasingly prevalent. We may therefore lay down the principle that the following operations undergone by a consignment on its journey will be considered not to affect its origin—*viz.*, unloading and reloading, changes in the mode of transport, bonding in Customs warehouses, free ports or free zones, external alterations in the putting up of the goods, division into lots or sorting, provided always that the origin appears clearly from the accompanying papers and that the above operations have taken place under official supervision and are attested in a satisfactory manner (by the Customs authority or the management of the bonded warehouses or free ports, etc.).

“One last point remains to be examined: so far we have considered goods originating in, or the *national* goods of, a given country. We have defined what is to be understood by the

origin or nationality of these goods, to what conditions this origin is subject and the influence which the conditions of consignment or transport may exercise over it. But there is also the case of goods imported into a State after having been *nationalised* in another country—*i.e.*, after having complied with Customs obligations and having entered into free circulation in that country. The legal provisions in this connection are not entirely concordant. Some States assimilate goods which have been nationalised in a country to goods originating in that country; others, while adopting the same assimilation, make it subject to certain reservations; others, on the contrary, still base themselves, although *sub conditione*, on the first origin of nationalised goods.

“Two considerations demand attention in this connection. In the first place, goods originating in a country not entitled to the most-favoured-nation clause should not be able to enjoy preferential duties by the devious method of previous importation into a country admitted to most-favoured-nation treatment. Secondly, we must consider the case in which goods originating in a country entitled to the clause, instead of being imported direct from the place of origin, first enter into free circulation in another country not entitled to the said clause. But, as has been stated above, the nationality of a product is determined by its origin, and this origin must be declared and, if necessary, proved.

“As regards consignments which do not proceed direct from the country of origin to the country of destination, it has been explained above what operations undergone on the journey are to be regarded as exercising no influence on the origin of the goods. But introducing the goods into the free market of a third country is not one of the operations authorised and should not be regarded as such, in view of the fact that the guarantees proposed (supervision and attestation by the official authorities) are not compatible with introduction to free traffic.

“The following principle therefore seems quite equitable:

“Goods which have entered the free traffic of a third country have the right to receive most-favoured-nation treatment if the country of origin and the third country are both admitted to the said treatment.’

“(2) Coming next to the question of what conditions, as regards their nature, the goods must fulfil in order to qualify for most-favoured-nation treatment, it may be observed that these

conditions are usually expressed by the words 'like' or 'similar' and sometimes by 'identical'. If these expressions are held to imply different standards, it must be admitted that the word 'like' is far preferable to the others, the expression 'identical' being the least desirable of the three, since the condition of identity may in practice involve a too restricted application of the clause, and is moreover too difficult to determine. However, the problem will not be solved merely by the use of one or other of these expressions. If we adopt the word 'like', we have still to decide what in practice is meant by 'like products'.

"The question has become extremely complicated and difficult, especially since the war; under the influence of protectionist tendencies, different countries have been endeavouring, in bilateral treaties concluded with each other, to create discriminations which are often of doubtful legitimacy.

"But here again it is difficult to determine without a thorough examination of all the facts how far these discriminations are justified by the actual nature of the goods, and how far they may be recognised, in the interests indeed of international traffic, since they sometimes offer a very valuable means of enabling the products of a given country to obtain reductions of duties or Customs facilities which could not be granted if they had to be extended to larger categories of goods.

"However, we may hope that the difficulties inherent in this question will be diminished with the introduction of the uniform Customs nomenclature on which the Economic Committee and the Committee of Experts have been engaged for so long.

"But what we are most concerned to declare is that, no matter what standards may be used to determine, in the case of a given category of goods, that these goods are 'like products', these standards must be applied in the same manner to all products of that category having their origin in any of the countries entitled to the benefit of the clause.

"In this connection, the following stipulations are clearly incompatible with the clause:

"(a) Provisions which restrict Customs privileges to products of a particular country or district simply because they originate in that country or district, thus ruling, *a priori*, that no other country can produce products like to those which it is sought to favour;

"(b) Provisions which make similarity depend on entirely

external characteristics or conditions which, by the very nature of things, only the products of given countries can possess or fulfil.

“For instance, when a country grants another country a reduction of Customs duties in respect of a given product, *provided the product in question is accompanied by an analysis certificate issued by a given authority* in the country to which the concession has been granted, but refuses to make the same concession to a third State on the ground that the latter cannot issue a certificate given by the authority indicated in the treaty, although equally qualified authorities might issue similar certificates, this would not be in keeping with the clause.

“When a country grants, in a bilateral treaty, some benefit to a product of the other contracting party, *provided this product is submitted to a given Customs office*, but refuses to accord this benefit to a third State whose products of the same kind cannot pass through the Customs office indicated in the treaty, though they might be submitted at other Customs offices equally competent to deal with the matter and to pass those goods through the Customs, this would also be contrary to the rule given in (b).

“It is understood, of course, that these examples are not intended to throw doubt on the right of the various countries to require, in certain cases, the submission of analysis certificates, or to stipulate in other cases that goods should pass through a given Customs office.

“Our only object in quoting these examples is to draw attention to the fact that the underlying principles of the clause distinctly prohibit the utilisation of such requirements for the purposes of unfair discrimination.”

“N. B.—*In thus expressing its view on “like products”, the Economic Committee felt that it was neither possible nor desirable to go too much into detail, owing to the wide variety of cases that actually arise. As the Governments of certain countries again raised the question of like products in the eleventh Assembly, the Committee thought that the best method to follow in reconsidering the question and deciding whether the opinion it had previously expressed required any modification would be to ask the Governments concerned for particulars of the specific cases in connection with which disputes or difficulties had arisen.*”

“The Governments of Denmark, Estonia, Finland, Latvia, the Netherlands, Norway, Sweden and Switzerland, to which it had

applied, showed by their replies that disputes with regard to the interpretation of the term 'like products' were not in reality very numerous, and that these cases added no new elements to those already within the Economic Committee's knowledge, on the basis of which it had drafted its above-mentioned commentary. All the cases quoted by the Governments as having given rise to difficulties were covered by the rules formulated by the Economic Committee in 1929. Hence, the latter did not consider it necessary to modify in any way the conclusions which it reached at that time.

"In the Committee's opinion, there can be no doubt that any dispute which may arise in this domain can be solved—at any rate, from the theoretical point of view, which is the only one that the Committee can adopt in dealing with this question—by applying the rule that it has laid down. A dispute might always arise as to the existence or absence of the intrinsic characteristics differentiating goods; but, as these characteristics naturally vary from one product to another, any endeavour to find a more precise formula than the Committee's and one which could be applied to all individual cases appears to be Utopian; and only expert examinations in each particular case could be decisive. Once the principle in question had been accepted by the different countries, it would be for the bodies provided for in commercial agreements for the settlement of disputes to which the clauses of these agreements might give rise to take a decision on the cases submitted to them for examination.

IV. *Exceptions to the Clause.*

"Having now stated the essential principles implied by the most-favoured-nation clause, its field of application and the objective qualifications which goods must possess to be entitled to most-favoured-nation treatment, we must observe that the clause, even in its unrestricted interpretation, cannot be made applicable to certain special situations, such as those resulting from a Customs union between two countries, or from traffic frontier zones.

"The strict maintenance of a Customs barrier between two adjacent countries is so clearly hampering to the inhabitants of the frontier districts, in regions where the frontier is not represented by some almost impassable physical obstacle, and an agreement allowing freedom of trade within a restricted zone on each side of the frontier is so manifestly justifiable, that an ex-

ception in favour of such traffic is something to which a third party, entitled in other respects to most-favoured-nation treatment, could not reasonably object. Accordingly, in most commercial treaties, allowance is made for the special situation in these districts by excepting the Customs facilities granted to frontier traffic from the most-favoured-nation regime.

“The clause is drawn up in different ways: latterly, there has been a very marked tendency to define the reservation more precisely. For instance, some recent treaties allow a contiguous State certain favours with a view to facilitating trade in particular frontier districts, not extending as a rule beyond 15 kilometres on either side of the frontier, besides granting privileges for the inhabitants of these districts.

“In one case—and indeed in several—the words for the inhabitants of these districts have been omitted, and we can quote at least one treaty where the zone in which facilities are granted to ‘*minor*’ frontier traffic is extended to 25 kilometres in certain exceptional cases. The following text is an example of less precise wording:

“... tariff concessions granted to neighbouring States solely with a view to facilitating frontier traffic in a limited zone on either side of the frontier.”

“In a certain number of treaties, including some of the most recent, the reservation does not appear at all.

“In short, the reservation, where it is employed, is of a more or less elastic character.

“In any case, it must be admitted that the exception concerning frontier traffic is rendered necessary, not merely by long-standing tradition, but by the very nature of things, and that it would be impossible, owing to differences in the circumstances, to lay down precisely the width of frontier zone which should enjoy a special regime. Hence we must be content to state that this exception is only legitimate and admissible if it is restricted to such limits as are essential to the attainment of its purpose—*i.e.*, to facilitating trade and in some cases also to rendering existence practicable for the inhabitants on either side of the frontier.

“The most-favoured-nation clause frequently includes a provision allowing for the possibility of each of the parties concluding a complete Customs union with a third Power. In such a case,

the economic unit becomes in practice something different from the political unit, and the Customs union may be regarded rather as the abolition of a Customs frontier than as a form of discrimination between competing foreign purveyors.

"In such cases, the exception to the most-favoured-nation clause takes the form of a reservation covering the privileges accorded to a third Power in virtue of a Customs union which has been or may hereafter be concluded. The clause may be drawn up in different ways, but the variations do not involve substantial differences. It appears in a large number of treaties.

"In regard to this point, it is sufficient to declare that Customs unions constitute exceptions, recognised by tradition, to the principle of most-favoured-nation treatment; but we do not propose in this paper to offer an opinion on the more controversial topic of their formation.

"Apart from Customs unions, it is necessary to consider the case of concessions which some countries grant one another on account of the special ethnic, historical, geographical or other ties which unite them (*e.g.*, the Iberian Clause, the Baltic Clause, the Scandinavian Clause, the South-American Clause, etc., and the special regime between Switzerland and certain zones of French territory).

"The exceptions falling within these categories could not be accepted as *implicit* by a mere reference; they must be expressly stated and their meaning and scope must be agreed to by the parties concerned.

"We should also bear in mind certain special arrangements under international treaties between countries or zones having particular economic interests in common, concluded to meet a provisional state of affairs (as, for instance, the present arrangement in German and Polish Upper Silesia and the Customs relations between Germany and the Saar Basin).

"As regards the question of preferential treatment granted to or by colonies, or to or by countries members of the same empire—a point appearing in various treaties—the Committee has refrained from investigating it in view of its political implications.

"But there is one question in regard to the colonies which might be usefully examined, apart from that of the preferential regime to which we have just referred.

"This question is as follows: Suppose that two countries have taken the most-favoured-nation clause as the basis of their rela-

tions in Customs questions, are native products of the colonies of one of these countries entitled to most-favoured-nation treatment when imported into the other country? In other words, does the clause apply also to products originating in the colonies?

“And conversely, are native products of one of the contracting countries entitled, on importation into the colonies of the other country, to the privileges accorded to the products of any third country (assuming, of course, that the latter is entitled to most-favoured-nation treatment)? In other words, does the clause also extend to goods imported into the colonies?

“In this connection, it should be observed that the provisions of commercial treaties, except where specially provided otherwise, are generally deemed to apply solely to the home country and that, when the above questions are answered in an affirmative sense, they are dealt with by special provisions in virtue of which the most-favoured-nation clause is given the necessary extension.

V. *Wording of the Clause.*

“The general considerations set forth above concerning the main principles of the clause, its field of application and the exceptions to it, enable us to put forward a standard form of clause which might be communicated to Governments, by way of example, for use in their bilateral conventions. But it is first necessary to offer a few observations regarding the selection of a standard form of clause.

“A study of the numerous examples which might be quoted would show that the most-favoured-nation clause takes the most varied forms in different treaties. When all allowance is made for the diversity of subjects which have to be regulated by this clause in bilateral conventions, it is seen that, even when the governing idea is substantially the same, the clause is worded in very different fashions. In some cases it is given a *positive* form (all advantages accorded to a third State are to be accorded to the other party); in other cases, it has a *negative* form (the other party is not to be subjected to less favourable treatment than that which is accorded to any third country). In other cases, again, it is fashioned *synthetically*, and again in other cases *analytically* and in detail; in some treaties there is a reference in general terms to most-favoured-nation treatment or to treatment on the basis of the most-favoured nation; finally,

in other treaties, we read that the favours, privileges, immunities, tariff reductions, etc., granted to any third Power are to be extended to the other party.

“These differences, and a vast number of others which might be quoted, cannot fail in the long run to work to the prejudice of international trade, which—more particularly in this field—needs rules which are clear, unequivocal, simple and intelligible to all.

“The elaboration of a single form of clause for Customs matters appears in these circumstances to be a work of the greatest utility.

“The question then arises whether it will be best to be content with an extremely simple and purely synthetic form of words merely declaring the intention of the contracting parties to grant each other most-favoured-nation treatment (leaving the actual scope of this guarantee to be elucidated in accordance with the rules for interpretation), or to adopt a rather more explicit style, stating the substantial provisions of the clause in direct terms in accordance with the principles we wish to see universally accepted.

“The former method, that of an extremely simple clause (such, for instance, as the following: ‘The two Contracting Parties undertake to grant each other most-favoured-nation treatment in all Customs questions’) would perhaps make it easier for everyone to adopt the clause. But it would have the objection of leaving open all questions connected with the scope of the most-favoured-nation clause and of making the positive value of the clause *wholly* and *exclusively* dependent on the rules for interpretation.

“For these reasons, we have thought it better to adopt the second method, which, though not obviating the need for common rules for interpretation, nevertheless makes it possible to find the solution of the above questions in the terms of the clause itself, leaving only a few special points to be elucidated by the rules of interpretation.

“The outcome of these considerations is the following formula, the terms of which are appreciably more explicit than those given above as an example. This formula is worded in general terms which may be adapted to meet special circumstances:

“The High Contracting Parties agree to grant each other unconditional and unrestricted most-favoured-nation treat-

ment in all matters concerning Customs duties and subsidiary duties of every kind and in the method of levying duties, and, further, in all matters concerning the rules, formalities and charges imposed in connection with the clearing of goods through the Customs.

“Accordingly, natural or manufactured products having their origin in either of the contracting countries shall in no case be subject, in regard to the matters referred to above, to any duties, taxes or charges other or higher, or to any rules and formalities other or more burdensome, than those to which the like products having their origin in any third country are or may hereafter be subject.

“Similarly, natural or manufactured products exported from the territories of either Contracting Party and consigned to the territories of the other Party shall in no case be subject, in regard to the above-mentioned matters, to any duties, taxes or charges other or higher, or to any rules and formalities other or more burdensome, than those to which the like products when consigned to the territories of any other country are or may hereafter be subject.

“All the advantages, favours, privileges and immunities which have been or may hereafter be granted by either Contracting Party, in regard to the above-mentioned matters, to natural or manufactured products originating in any other country or consigned to the territories of any other country shall be accorded immediately and without compensation to the like products originating from the other Contracting Party or to products consigned to the territories of that Party.

“Nevertheless, the advantages now accorded or which may hereafter be accorded to other adjacent countries in order to facilitate frontier traffic, and advantages resulting from a Customs union already concluded or hereafter to be concluded by either Contracting Party, shall be excepted from the operation of this article.”

(c) RELATIONS BETWEEN BILATERAL AGREEMENTS BASED ON THE MOST-FAVOURLED-NATION CLAUSE AND ECONOMIC PLURILATERAL CONVENTIONS.

“During the Diplomatic Conference held at Geneva to draw up an International Convention on the Abolition of Import and Ex-

port Prohibitions and Restrictions, the question arose whether States not parties to that Convention could, by virtue of bilateral agreements based on the most-favoured-nation clause, claim the benefit of any advantages mutually conceded by the signatories of the International Convention. In deference to this consideration, it was even proposed to include a clause to that effect in the Convention. It was soon realised, however, that this question could not be answered in the Convention, which could not affect the contents of bilateral agreements based on the most-favoured-nation clause. The Conference realised the great importance of the problem, both for the general economic work of the League and for the conclusion of future economic agreements under the League's auspices, and the nature and field of application of such agreements. It was urged at the Conference that the conclusion of plurilateral conventions would be hindered if countries, while not acceding to such agreements, could still, without giving any counter-engagements, avail themselves of the engagements undertaken by the signatory States of such conventions.

"The Economic Committee of the League was asked to make an exhaustive study of the most-favoured-nation clause in commercial treaties and to put forward proposals regulating it in as comprehensive and as uniform a manner as possible, and it has carefully considered the question, which is the subject of the present report. It took the view that the World Economic Conference of Geneva, when it recommended the conclusion of plurilateral economic conventions with the object of improving the world economic situation and the application of the most-favoured-nation clause in the widest and most unconditional form, probably did not quite realise that—up to a point—these two recommendations might clash. One argument—and a very sound one—brought up in the Economic Committee was that in certain cases countries would have little or no interest in acceding to a plurilateral economic convention or in undertaking the commitments it entailed if, by invoking the most-favoured-nation clause, as embodied in bilateral agreements, they could claim as of right and without incurring corresponding obligations, that the obligations contracted by the signatory States of the plurilateral convention should apply to themselves. It was strongly urged, indeed, that such possibility might seriously impair the whole future economic work of the League, and that the

only means of averting the danger would be to adopt a provision whereby the most-favoured-nation clause embodied in bilateral commercial treaties would not, as a rule, affect plurilateral economic conventions.

"It was objected, however, that a clause of this kind, instead of leading, as the World Economic Conference recommended, to the unlimited application of the most-favoured-nation clause, would actually check it, and that, more especially in countries where the unlimited application of this clause is the basis of commercial relations with foreign countries, such a reservation would probably be misunderstood and might give rise to a hostile attitude towards the League's economic work. It was further argued that a State might quite conceivably, on wholly serious and genuine grounds, be unable to undertake the commitments involved by an international economic convention; that the final decision whether it could so do or not would lie with the State itself; and that it could hardly be asked, as a result of a most-favoured-nation clause drafted *ad hoc* in bilateral commercial treaties to give up the right in cases of this kind to refuse to accept differential treatment on the part of one or more other States.

"The arguments advanced on both sides are so cogent that the Economic Committee has not found it possible at this moment to find a general and final solution for this difficult problem.

"It is unanimously of opinion, however, that, although this reservation in plurilateral conventions may appear in some cases legitimate, it can only be justified in the case of plurilateral conventions of a general character and aiming at the improvement of economic relations between peoples, and not in the case of conventions concluded by certain countries to attain particular ends the benefits of which those countries would, by such a procedure, be refusing to other States when the latter might, by invoking most-favoured-nation treatment, derive legitimate advantages.

"The said reservation should also be expressly stipulated and should not deprive a State not a party to the plurilateral convention of advantages it enjoys either under the national laws of the participating State or under a bilateral agreement concluded by the latter with a third State itself not a party to the said plurilateral Convention.

“Finally, this reservation should not be admitted in cases in which the State claiming the advantages arising under the plurilateral convention, though not acceding to it, would be prepared to grant full reciprocity in the matter.

“The Economic Committee expresses the view that countries which, with reference to the terms of plurilateral economic conventions, agreed to embody in their bilateral agreements based on the most-favoured-nation clause a reservation defined in accordance with the principles set forth above would not be acting contrary to the recommendations of the World Economic Conference of Geneva, and consequently will not be acting in a manner inconsistent with the objects which the League has set itself to attain.”

ANNEX II

MEASURES TO PREVENT THE GROWTH OF VESTED INTERESTS BEHIND QUANTITATIVE TRADE CONTROLS DURING THE POST-WAR TRANSITIONAL PERIOD OF GENERAL SHORTAGE.

Note by the Secretariat

1. The purpose of this note is to consider what measures might be adopted by governments to prevent the growth of vested interests in the maintenance of quantitative restrictions on trade during the post-war transition period.¹ During the war the trade of practically all countries has been subjected to quantitative restrictions and exchange controls. The trade of many has been subject to the restrictions imposed by blockade. There is little probability that many countries will be in a position to change suddenly from this condition of restriction and regulation to one of a simple price economy. On the contrary, most countries will be anxious to husband their foreign exchange resources and; during the period of scarcity both of foreign exchange and of goods, to give preference to the import of those goods which are most essential for the revival of peace-time economic life and least easily produced at home. We must anticipate, therefore, that quantitative restrictions of one sort or another will remain in operation for some time, the length of which will vary from country to country.

But, if it is the desire of governments to develop a free-price economy and expand multilateral trade later, then it is important that vested interests in the maintenance of quantitative controls should not be allowed to develop during the transition period. Such vested interests may take the form (a) of the assumed right to an abnormal rate of profit, such as that which a merchant may reap from the receipt of a quota when the total quota for any commodity is so small that there is a wide discrepancy between the price at which he can purchase that commodity abroad and the price at which he can sell it at home. Such abnormal profit expectations may in certain cases lead to the issue of additional shares by a benefiting company.

The vested interests may furthermore lead to (b) the investment of additional capital in fixed plant and the training and employment of additional workers when, owing to the import restrictions, domes-

¹ The note is not concerned with abnormal profits arising out of cartel and similar private agreements, even though these agreements may be facilitated by quantitative restrictions. The control of such profits raises problems of quite a different order from those considered here.

tic firms find that their home demand outruns their productive capacity. Whatever form they take, these vested interests will render it more difficult for governments to remove the quantitative restrictions.

2. In considering this problem it is well to distinguish between the vested interests of merchants, which can only take form (a) above, and those of producers, which may take either form (a) or form (b).

3. The Economic and Financial Committees, at a meeting held in December 1943, made the following recommendations with reference to the prevention of undue profits by merchants :¹

"It is . . . of the great importance that while controls are in force, vested interests in their maintenance should be prevented from growing up. If such vested interests are allowed to develop and the trading community is placed in a situation under which its profits will be reduced by an expansion of trade or by the abandonment of direct controls, then the chances of realizing this second objective of the Atlantic Charter and the Mutual Aid Agreements will be seriously jeopardized.² Any system of restricting imports by means of licenses involves the danger of the recipient of the license making an abnormal profit on the goods he is allowed to place on the home market. After the last war, as we have seen, the problem was not solved; the vested interests were created and tariffs were raised in order to equalize the effect of quantitative controls when they were removed. It would be in flagrant contradiction with Article 7 of the Mutual Aid Agreements if action to raise tariffs in this way were to be taken after the present war.

"There are three main methods by which this difficulty may be overcome. The first is to create or retain government monopolies which would in fact eliminate private trading profits. The second is to remove abnormal profits by taxation or other means. The third is to maintain domestic price control over all licensed goods.

"The first of these methods requires but brief comment. The trader would under a state monopoly become in effect the agent of the government and occasion for abnormal profit would be effectively elimi-

¹ *Report to the Council on the work of the 1943 Joint Session.* (Doc.C.I.M.I.1944.II.A.).

² It is of interest to note, in this connection, the following resolution adopted by the Atlantic City Conference of 1943.

"That the government or recognized national authority which exercises administrative authority in the area should take appropriate measures to insure that insofar as the distribution within a liberated territory of relief and rehabilitation goods is done through private trade, the remuneration earned by private traders for their services is no more than is fair and reasonable." (Resolution No. 7, Relief and Rehabilitation Policies—Part II, Resolutions on Policy of the First Session of the Council, UNRRA.)

nated. Such a system involves, however, the risk of sapping the vitality of the trading community and thus rendering the reversion of functions to it difficult and hazardous. It involves also all those disadvantages and dangers to international relationships that we have just enumerated.

"The second is theoretically attractive and has in fact been applied in the past in a number of countries. In practice, however, it is difficult to adjust the tax or fees so as to absorb all the abnormal profit that may be made.

"It may be rendered unnecessary if the third method can be applied—that is to say, if domestic prices are through control kept aligned to c.i.f. prices port of arrival; and when this is not the case but domestic prices are controlled at some level above those abroad, the determination of the correct license fee is of course greatly facilitated.

"No system is likely to prove perfect in practice; but we would urge that on the one hand every endeavour should be made to prevent the accrual of abnormal profits to the recipients of import or export licenses and on the other that governments should refrain from increasing their tariffs as the counterpart to relaxing trade controls. Only if such restraint is exercised and time afforded to formulate long-term commercial and tariff policies in the light of the post-war situation can we hope for the early realization of the agreed objectives."

4. The problem of the growth of vested interests amongst producers presents greater difficulties. It will be necessary to consider industry and agriculture separately, and to take into consideration also the possibility not only of import, but also of export restrictions.

5. Should any country contemplate not only re-establishing multilateral trade but also an extension of its free trading area by forming a customs union, then additional problems present themselves. We revert to this rather special case of customs unions in section 9 below. The various proposals made below with reference to the simple case of the restriction of multilateral trade under a free price economy would apply to them, though require possibly to be supplemented by other measures.

6. Four classes of measures arise for consideration in all cases. First, those relating to commercial policy; secondly, fiscal measures; thirdly, government control of prices, either by price fixation or by government monopoly of sale and purchase, and, fourthly, control of investment.

7. We shall consider commercial policy first.

It would seem obviously desirable that governments should, imme-

diately on the cessation of hostilities, make a declaration of their policy with reference to tariffs—that, for instance, they do not intend to increase or that they intend to decrease the existing rates as soon as conditions permit.

Can they go farther or act earlier? Would it be useful, as was suggested at Atlantic City, to conclude a convention before the end of hostilities under which governments undertook not to increase their tariffs either while the quantitative controls are in force or for a specific period of time? Such a convention would be useful if and only if the breathing space it afforded were utilized for the elaboration of further agreements between states with reference to tariff reductions or consolidations. Were this not done, then the initial convention is really dependent upon whether there are grounds for believing that governments are likely to be seriously prepared at some not too distant date after the termination of hostilities to adopt a more liberal commercial policy than they did before the war and at least a policy which is not less liberal than in the late 'twenties.

However this may be, it is certain that conventions of this character will not be sufficient to prevent the growth of vested interests during the period of the quantitative restrictions. At best, they will not have more than a certain deterrent effect. How important that effect will be will depend on the extent to which the business world believes that the government is genuinely bent on carrying out its intention and that a change of policy is not likely to follow a change in government. In any case, more than this is necessary.

8. Within certain limits, both as regards the scope of operations and their duration, price control and the control of consumption may be employed to check the growth of vested interests. This question is dealt with in the report of the Delegation on Economic Depressions entitled, "The Transition from War to Peace Economy,"¹ and the following extracts from that report are relevant:

Consumers' Goods

"Direct control of consumption during the war takes various forms but four are of major importance: first, direct rationing of the final consumer; secondly, special permits granted to individual consumers on proof of need; thirdly, what is known as point rationing of the consumer; fourthly, rationing or some other form of direct control over the producer and distributor."

¹ League of Nations (doc.C.6.M.6.1943.II.A.).

“ . . . the right procedure in the case of straight rationing is, gradually and as rapidly as possible, to increase the rations as the supplies coming forward increase. If the government purchases the crude product and fixes prices at all stages up to the final retailers' price, there should be comparatively little difficulty. . . . Granted that rations are not raised more rapidly than the supplies, there should be no underlying tendency towards higher prices, but on the contrary, as the needs of one income group after another are satisfied, a tendency for prices to fall. As soon as prices have fallen below the fixed maxima, those maxima may be abolished.”

“The permit system . . . presents no special difficulties. Permits will require to be more liberally granted as supplies increase and, in the case of goods bought by all, may, when supplies suffice to justify such a step, be replaced by coupon rationing.

“Point rationing . . . is normally applied to semi-durable goods such as clothes, though it is being increasingly applied also to certain food-stuffs. . . . Here again . . . the right procedure is not to abolish the system suddenly but to increase the number or the purchasing power of coupons.”

“The problem of price decontrol under a point rationing system is somewhat complex. . . . the government can adopt four courses:

(a) It can change the coupon values in the manner widely adopted during the war.

(b) It can change the fixed prices or abolish the price maxima.

(c) It can exclude the goods in plentiful supply from rationing which would automatically raise the value of the points in terms of the remaining rationed goods.

(d) It can attempt to increase the supply of the goods in great demand by, for instance, its allocation of raw materials or tonnage.”

Investment Goods

“ . . . to fix the price of all the goods offered for sale in peacetime is scarcely possible. The variety of manufactured goods is so great that the administration of any such control presents almost insuperable difficulties. A similar difficulty presents itself with regard to the narrower range of products required for productive processes.”

Raw Materials

“The quantitative raw material controls instituted during the war have taken four interlocking forms: (a) government purchase, (b) tonnage control, (c) control of international trade, and (d) some system of allocation to consuming firms, through direct quota, priorities, licenses to purchase, etc. These quantitative controls are normally accompanied by price control.

"So long as the supply of tonnage or of raw materials is seriously short . . . these controls must . . . be maintained in some measure. This implies the maintenance of the government's preference schedule in place of the public's. But we have to recognize that the determination of that schedule in peacetime will become increasingly difficult. So long as the government is itself the final consumer of a very large proportion of the raw materials it controls or so long as the public is directly rationed, it is relatively easy to estimate the total amount of raw materials that each industry and finally each firm will require. But when the future demand for the final product will be determined by an as yet unexpressed consumers' choice, the risk of error is obviously enormously magnified."

"There is . . . much to be said in favour of removing price controls from raw materials not mainly entering into rationed consumers' goods at the earliest possible moment. To fix the prices of all the infinite range of commodities offered to the public for sale in peacetime is . . . likely to prove impossible. . . . To fix the prices of the raw materials alone . . . gives to the manufacturer fortunate enough to secure them a wind-fall profit without necessarily having any great effect on the price of the consumers' goods."

"In spite of these difficulties we do not believe that the immediate decontrol of the prices of this class of raw materials would be practicable."

"In view of all these considerations, we conclude:

(a) That the rationing of raw materials not made into rationed goods may have to be maintained for some time after the cessation of hostilities and maximum prices on these goods retained.

(b) That governments may frequently find it advisable to leave each trade to carry out the rationing of individual firms under government supervision. . . .

(c) That as soon as there are grounds for believing that the risk of runaway prices is past, such controls should be abolished, commodity by commodity."

It will be seen from the foregoing quotations that the policy of price control is relatively simple when the goods consumed by the final consumer are simple in nature and are rationed, but that it is not a policy that can be universally applied, nor is it likely to be generally successful once rations have been abolished. It is more practicable with regard to food than in the case of other products. The question of agriculture is dealt with in section 10 below.

Even when or where price controls are not practicable the government may exercise some influence over prices and prevent monopolists or quasi-monopolists from reaping undue profits by increasing the

import quotas. While these import quotas constitute an instrument which may be used on occasions, however, their utilization for this purpose cannot be general or the scope of its influence very wide.

9. None of the measures considered so far, therefore, seem likely to have a general or sufficiently permanent influence. There remain for consideration, so far as industry is concerned, fiscal measures and investment control.

We are considering conditions under which the domestic producer is likely to reap an abnormal profit on account of the cutting off of foreign competition. This abnormal profit is likely to result in (a) a great unwillingness on his part (and on the part of labour) to see the restrictive measures to which it is due abandoned, and consequent political pressure to maintain the restrictive measures, and (b) an investment of new capital in enterprises which would not be able to withstand foreign competition if and when the restrictive measures are abandoned. Can any form of tax be devised which would prevent the growth of these abnormal profits and the consequences just described without unduly hindering enterprise?

The profit arises on account of the difference between the prices at which goods can be sold on the domestic market when foreign competition has been eliminated or reduced and the prices at which they can be produced. The quantitative restrictions are equivalent to a tariff, the height of which can be measured by the difference between the prices at which domestic goods are actually sold and the prices at which foreign goods could be sold on the domestic market. If from this difference are deducted the existing tariff rates, we arrive at the surcharge on those rates that the quantitative restrictions represent. The problem is to impose a tax equivalent to this surcharge, or as nearly equivalent as possible without unduly hindering enterprise.

The essential elements of the problem are summarized in the following table:

	WHEN TOTAL PRODUCTION AMOUNTS TO		
	x	x + y	x + y
		I.R.	C.R.
Domestic Sales Price	150	140	140
Foreign Price plus Domestic Tariff	100	100	100
Abnormal Profit = Tax	50	40	40
Net Sales Receipts after paying Tax	100	100	100
Cost per Unit	90	85	90
Profit per Unit	10	15	10

Note: I.R. = increasing returns; C.R. = constant returns.

The first column shows the various factors when total production equals any initial amount, x . The second column shows the assumed effect of increasing production from x to $x + y$ when the commodity is produced under conditions of increasing returns. It will be noted that the cost per unit falls from 90 to 85. The domestic sales price likewise falls on account of the greater number of the goods in question placed on the market. The third column shows the effect of increasing the production from x to $x + y$ when the commodity is produced under conditions of constant return. In this case the cost per unit remains unchanged at 90; but the sales price falls as in the previous case, and for the same reason.

Were a tax imposed on each unit of production equivalent to the difference between the sales price and the foreign price plus domestic tariff, that is, equivalent to the surcharge which the quantitative restrictions represent, then,

(a) When the commodity is produced under conditions of increasing returns, it pays the manufacturer to increase output and reduce price, because his cost before the tax is reduced by an amount equivalent to the reduction in the sales price. A tax of this sort should, therefore, always prevent a monopolist from opting in favour of a smaller output and higher price, rather than a larger output and lower price, when such option exists. It would, moreover, permit profits to increase as output increased, while preventing the special profits resulting from the quantitative restrictions from accruing to the manufacturer.

(b) When the commodity is produced under constant returns, however, such a tax affords no special inducement towards increasing output. Such a tax would, therefore, be more far-reaching in its effects in the case of industry than in the case of agriculture.

It should be noted that the incidence of the tax could not fall on the consumer, for were the tax added to the price, the tax itself would be proportionately increased.

But the elaboration of such a tax presents very considerable difficulties:

(a) The sales price must be the sales price to the final consumer, and not the price at which the manufacturer sells to a middleman. For were the latter selected and each manufacturer taxed on the basis of his own books, collusion between the manufacturer and the middleman would be difficult to prevent. Moreover, the middleman, if there were no collusion, would reap an undue profit.

(b) Exact comparisons between the import price and the sales price will always be difficult and sometimes impossible, for the im-

ported goods will not be identical with the home-produced goods. In some cases they may be imported as parts or in an unfinished state.

(c) Both domestic and foreign prices will constantly change, and indeed during this period may be in a state of flux. Fairly frequently changes in the rate of the tax will therefore be necessary. It would probably prove simplest to fix the rate as a percentage of average import prices, effecting changes at definite intervals, for instance, every year or every six months.

But at best, nothing more than a rough approximation to the ideal rate can be attained, and in view of the danger of checking enterprise during a very difficult time, it would clearly be wise to fix a rate rather too low than too high. This is the more necessary in view of the great difficulties with which industrial entrepreneurs are likely to be faced in any case during the transition period. It is necessary to view such a tax, therefore, as a means for preventing fortuitous profit being reaped or bad investments being made by certain producers as a result of government action, and not in any way as an instrument for imposing additional fiscal charges on enterprise as a whole. Indeed, if practical at all, it would seem to have most chance of success if adopted as a modified form of excess profits tax where such tax already exists.

10. A tax of the type that we have been discussing would prove to be somewhat less effective in the case of agriculture. Agriculture differs from industry both on account of the fact that it is more likely to be subject to constant or decreasing than to increasing returns, and secondly, owing to the fact that monopoly profits are much less common. As a rule, the unit of production, the farm, is small, and no individual producer can, by keeping off the market, affect the market price. The market price, in the case of agricultural products, is likely to reflect much more accurately the play of demand and supply. This being so, the tax loses its merit as a means for forcing the producer to sell more at a lower, rather than less at a higher price; the producer will do so in any case, except where inflationary conditions obtain. The tax could, however, be adapted so as to allow an increased profit per unit as production increased, and this system could be employed to direct production towards those crops which the government was anxious to favour.

Moreover, though this tax loses some of its merits in the case of agriculture, it is easier to apply. Agricultural products are fairly uniform in nature, and it is consequently easier to determine both the import and the domestic sales price.

An alternative policy for agriculture would be for the government

to establish a monopoly for the purchase and sale of all agricultural products. It could then keep the price to the farmer as low as it wished, and the price to the consumer at a level somewhat below the farmer's price, if products were imported from abroad at lower prices. Again, in the case of such a monopoly, the government could easily direct production in whatever manner it desired by modifying the relative prices that it offered for different crops. Price differentials of this character are much more effective than acreage control.

In fact, however, the government will be faced by the inevitable difficulty that during the shortage period it wants to stimulate (or maintain) domestic production, and costs are likely to rise (or to have risen) as more and worse land is brought under the plough. The government must therefore offer a price adequate to cover this increase, and all owners of better land will reap larger profits.

This difficulty could theoretically be overcome by a progressive tax on economic rent. But in practice, the economic rent, especially when the farmer owns his own land, is unascertainable. To some extent, no doubt, the abnormal profit could be absorbed by a progressive income tax. But such a tax is a very crude instrument for the purpose, for there are but small grounds for assuming that the farmer with the largest income will benefit most from the quantitative restrictions. In view of this consideration, the tax proposed in section 9 above would seem to be more appropriate than a progressive income tax, though far from perfect.

Where agriculture has been subsidized during the war and the desired production during the post-war period of shortage can only be attained with some subsidy or as a result of quantitative restrictions, the subsidy itself can be used as an instrument both against vested interests and in favour of those crops which the government desires to promote. By reducing the subsidy the government can remove part of the war-time abnormal profits. By removing it on one crop, wheat, for instance, and increasing it on another crop or product, milk, for instance, it can adapt agriculture gradually to the form which would be best fitted to meet foreign competition when multi-lateral trade is re-established. But such a policy is subject to two serious limitations. First, it is difficult under any subsidy system to prevent the farmer on the most favourably situated land from obtaining an abnormal profit (rent); secondly, in all countries in which the national income has been greatly reduced as a result of the war, it will be difficult—and it may be unjustifiably extravagant—to divert demand from such cheaper foodstuffs as cereals, which constitute the

most important items in international trade, to the more expensive foods such as meat or milk.

11. The measures that have been considered up to this point are mainly directed to preventing vested interests in abnormal profits from arising and thus indirectly checking any tendency towards the investment of new capital in enterprises which would not be able to compete were the quantitative restrictions removed. There is much to be said in favour of direct control of capital investment during the transition period. Capital will be scarce, and all wasteful investment should be avoided. However, the desirability or undesirability of central control of private investment during the transition period must depend to a very large extent upon the competence of the administrative machinery of the government. On the details of all projects the business man and the farmer are in a much better position than the government to form a judgment. All that the government can do is to prevent capital being directed towards purposes which, in the government's view, either on account of considerations of social policy or in the light of the government's own intention regarding economic policy, or in the light of the information at its disposal concerning private investment in different branches of industry, would not seem likely to prove advantageous. If the government is not perfectly clear about its own intentions for the future, or if its machinery is slow and cumbersome, so that delays are involved, then it is very questionable whether investment control would prove beneficial. But in the case of a government which has committed itself to form a customs union, one major factor in its economic policy is known and may be so important as to justify investment control even when it would not be justified otherwise. We may turn, therefore, at this point to this second class of countries mentioned in the fifth paragraph of this memorandum, namely, those which propose to form a customs union.

12. The danger of vested interests growing up during the period of quantitative restrictions is greater in the case of these countries until the union comes into force because the differential between the artificial domestic price caused by these restrictions and the prices which will finally rule after the formation of the union is likely to be greater. We may assume for purposes of presentation four hypothetical strata of prices:

- (a) the artificial price caused by the quantitative restrictions;
- (b) the price that would be caused by the existing tariff were it the operative factor;
- (c) the price that would be caused by the tariff after it has been

modified as a result of the conclusion of the customs union. We may assume that this union tariff never imposes higher average duties on the whole new customs area than heretofore; but the tariff of one member (or even more than one) may be raised.

(d) the price caused by the above, and by the total abolition of the tariff between the country in question and the other parties to the customs union.

Obviously, if price (d) is not lower than price (b) a special problem only arises as regards those commodities in which the intra-union competition is likely to be serious. But as a rule (d) will be lower than (b) not only on account of the abolition of the tariffs among the members of the union but because price (c) will be lower than price (b). Cases may arise in which a country on entering such a union may raise its tariff because it is so much lower than those of the other members who reduce theirs that it will not prevent the new common tariff being lower for the whole trading area than it was before. But such a case must be the exception rather than the rule if the customs union is to be accepted by third parties—an exception, moreover, which presents no special problem in this connection. We may confine ourselves in this consideration of broad principles, then, to the problem of the adaptation of price (a) to price (d). We must consider whether the measures already suggested are adequate to cover the necessary ultimate adaptation to price (d). Obviously all these measures are appropriate in this case; the only question is whether they are adequate.

As already stated, the case for investment control becomes a strong one; for on the one hand, the intention of the government is known, and on the other, the shock to the whole system which the ultimate adaptation will involve is greater, and the risk of loss on account of ill-advised investment is likewise greater.

But the government's intention may be either general or specific. It may be known that the government will have to reduce its tariff in order to form the union proposed, or the government may have come to a definite understanding as regards the reduction to be made. Obviously, the business man will be much better placed in deciding what investments he should make if the government has published the new rates. This being so, there would seem to be every advantage in the government's concluding its agreement at the earliest possible date, even though the agreement may not come into force until some subsequent date.

The fact that the tariff with the other parties to the union will be

ultimately abolished altogether, is of course known, once the union has been approved in principle. In this case, therefore, the producer is fully informed, and the political danger of vested interest is eliminated. The problem that presents itself is whether the government can do anything to cushion the shock of the ultimate adaptation of prices to the (d) level.

Obviously, there are two courses of action open. The first is to prevent the (a) price, the price resulting from the quantitative restrictions, from becoming too high; the second is to prevent the (d) price, the price resulting from the abolition of the tariff, from becoming too low.

The first result might be achieved by allowing the quota for the import of goods which the other parties to the customs union are likely to supply to be relatively large. This would be facilitated if a monetary agreement had been concluded between the two parties to the projected union, each country mutually guaranteeing the other's currency.

The second result might be attained if, in the monetary agreement, the country which had to reduce its tariff down to or toward the level of the other countries' tariffs were allowed slightly to undervalue its currency.

13. Up to this point we have assumed that importers and producers are liable to reap a special benefit on account of exceptional quantitative restrictions on imports. The fact must not be overlooked, however, that they may suffer a loss from quantitative restrictions on exports. When the exports of any particular commodity are restricted it would be difficult in fact to prove that any abnormal profit is being or can be reaped from an import restriction on that commodity. For if the import restrictions raise the domestic price of a commodity above the world level exports will not take place excepting on a dumping basis. If the situation is such that exports of that commodity would not take place, there is no purpose in imposing the export restrictions on it, and they should be abolished. If exports could take place by selling cheaper abroad than at home owing to the economy of a larger turnover, then the potential exporter does suffer from the export restriction and it would be inequitable to tax him on account of the benefit he derived from the import restriction. It is true that theoretically the benefit from the import restriction may exceed the loss from the export restriction. But as the loss cannot be calculated, this fact is of little practical importance.

ANNEX III

SHORT LIST OF IMPORTANT LEAGUE OF NATIONS DOCUMENTS RELATING TO TRADE AND COMMERCIAL POLICY¹

I. INTERNATIONAL CONVENTIONS IN FORCE, WITH DOCUMENTS RELATING THERETO

Customs Formalities

International Conference on Customs and other Similar Formalities, Geneva, October-November 1923:

Proceedings of the Conference, 2 vols. (C.66.M.24.1924.II.)

Index to the Proceedings of the Conference. (C.66(b).M.24(b).1924.II.)

International Convention relating to the Simplification of Customs Formalities, and Protocol. (C.678.M.241.1924.II.)

Application of the International Convention (Measures taken by Governments to give effect to the provisions of the Convention) : (E.268.)

Nine series of Summaries Communicated by Governments in Execution of Article 9, 1926-1936. (C.354.M.127.1927.II.) (C.180.

M.56.1928.II.) (C.126.M.42.1929.II.) (C.539.M.193.1929.II.)

(C.183.M.85.1930.II.) (C.557.M.223.1930.II.) (C.227.M.95.1931.II.B.) (C.270.M.140.1933.II.B.) (C.226.M.138.1936.II.B.)

Application of Articles 10 and 11 of the Convention: (C.198.M.75.1929.II.)

Seven Series of Summaries, 1929-1937. (C.563.M.224.1930.II.)

(C.913.M.479.1931.II.B.) (C.698.M.335.1932.II.B.) (C.321.M.165.1935.II.B.) (C.478.M.254.1935.II.B.) (C.186.M.132.1937.II.B.)

Commercial Arbitration

Protocol on Arbitration Clauses, Geneva, 1923. (A.83.1923.II.Annex.)

Convention on the Execution of Foreign Arbitral Awards, Geneva, 1927. (C.659(I).M.220(I).1927.II.)

Export Prohibitions and Restrictions

International Agreement relating to the Exportation of Hides and Skins. (C.11.M.8.1929.II.)

¹ An annotated and fuller list is contained in the *Catalogue of Selected Publications on Economic and Financial Subjects* issued by the League in 1943.

International Agreement relating to the Exportation of Bones. (C.12. M.9.1929.II.)

Bills of Exchange, Promissory Notes and Cheques

Convention Providing a Uniform Law for Bills of Exchange and Promissory Notes (with Protocol, Annexes and Final Act). (C.346. M.142.1930.II.)

Convention for the Settlement of Certain Conflicts of Laws in Connection with Bills of Exchange and Promissory Notes (with Protocol). (C.347.M.143.1930.II.)

Convention on the Stamp Laws in Connection with Bills of Exchange and Promissory Notes (with Protocol). (C.348.M.144.1930.II.)

Convention Providing a Uniform Law for Cheques (with Protocol and Annexes). Geneva, March 19th, 1931. (C.458.M.195.1931.II.B.)

Convention for the Settlement of Certain Conflicts of Laws in Connection with Cheques (with Protocol). Geneva, March 19th, 1931. (C.459.M.196.1931.II.B.)

Convention on the Stamp Laws in Connection with Cheques (with Protocol). Geneva, March 19th, 1931. (C.460.M.197.1931.II.B.)

Veterinary Police Regulations

International Convention for the Campaign Against Contagious Diseases of Animals. (C.77.M.33.1935.II.B.)

International Convention Concerning the Transit of Animals, Meat and Other Products of Animal Origin. (C.78.M.34.1935.II.B.)

International Convention Concerning the Export and Import of Animal Products (Other than Meat, Meat Preparations, Fresh Animal Products, Milk and Milk Products). (C.79.M.35.1935.II.B.)

Commodity Agreement

International Sugar Conference, London, 1937. Text of the Agreement, and Proceedings and Documents of the Conference. (C.289. M.190.1937.II.B.)

II. DRAFT INTERNATIONAL CONVENTIONS AND CONVENTIONS NOT IN FORCE, WITH DOCUMENTS RELATING THERETO

Import and Export Prohibitions and Restrictions

Proceedings of the First Conference for the Abolition of Import and Export Prohibitions and Restrictions. (C.21.M.12.1928.II.)

International Convention for the Abolition of Import and Export

Prohibitions and Restrictions. Protocol to the International Convention. Annexed Declaration. (C.14.M.11.1929.II.)
Proceedings of the Second Conference, 1928. (C.611.M.187.1928.II.)
Supplementary Agreement to the Convention. (C.13.M.10.1929.II.)
Proceedings of the Third Conference, 1929. (C.176.M.81.1930.II.)

Tariffs

International Conference for the Conclusion of a Tariff Truce. Preliminary Draft Convention drawn up by the Economic Committee. (C.519.M.177.1929.II.) (C.I.T.D.1.)
Commercial Convention, with Protocol, of March 24th, 1930. (C.203.M.96.1930.II.)

Treatment of Foreigners

Proceedings of the International Conference on the Treatment of Foreigners, 1929. (C.97.M.23.1930.II.)
Preparatory Documents for the Conference (including the Draft International Convention prepared by the Economic Committee). (C.36.M.21.1929.II.)

Commercial Propaganda

Draft International Agreement for the Purpose of Facilitating Commercial Propaganda. (E.881.) (1935.II.B.5.)

III. MODEL BILATERAL TREATIES AND INTERNATIONAL STANDARDS

Double Taxation and Fiscal Evasion

Model Bilateral Conventions for the Prevention of International Double Taxation and Fiscal Evasion. (C.2.M.2.1945.II.A.)

Most-Favoured-Nation Clause

Recommendations of the Economic Committee relating to Tariff Policy and the Most-Favoured-Nation Clause. (E.805.) (1933.II.B.1.) (Relevant Sections Reproduced in Annex I above)

Procedure for Settlement of International Economic Disputes

Memorandum relating to the Pacific Settlement of International Disputes concerning Economic Questions in General and Commercial and Customs Questions in Particular. (E.666.) (1931.II.B.1.)

Procedure for the Friendly Settlement of Economic Disputes between States, set up by a Resolution of the Council of January 28th, 1932. (C.57.M.32.1932.II.B.)

Tariff Nomenclature

Revised Draft Customs Nomenclature. 2 vols. (C.295.M.194.1937.II.B.)

Unfair Commercial Practices

Economic Committee: Report to the Council on the Work of its Thirty-Seventh Session, 1932. Appendix II. (Bribery and Unfair Commercial Practices) (C.74.M.39.1932.II.B.)

Veterinary Police Regulations

Economic Committee: Report to the Council on the Work of its Fiftieth Session, 1939. (C.178.M.107.1939.II.B.) Appendices I-III: International Rules concerning the Export and Import of Live Animals.

Provisions for an International Sanitary Convention on the International Commerce in Meat and Meat Preparations.

International Rules relating to Methods for the Inspection of Meat intended for International Trade.

IV. REPORTS AND STUDIES RELATING TO TRADE POLICY

General

The Transition from War to Peace Economy: Report of the Delegation on Economic Depressions. Part I. (C.6.M.6.1943.II.A.)

Economic Stability in the Post-War World. The Conditions of Prosperity after the Transition from War to Peace. Report of the Delegation on Economic Depressions. Part II. (C.1.M.1.1945.II.A.)

Commercial Policy in the Interwar Period: International Proposals and National Policies. (1942.II.A.6.)

Trade Relations between Free-Market and Controlled Economies. (1943.II.A.4.)

Observations on the Present Prospects of Commercial Policy. (C.179.M.108.1939.II.B.)

Remarks on the Present Phase of International Economic Relations (September 1937). (C.358.M.242.1937.II.B.)

International Financial Conference, Brussels, 1920:

Vol. I. Report of the Conference and Resolutions of the Commissions.

Vol. II. Verbatim Record of the Debates.

Vol. III. Statements on the Financial Situation of the Countries Represented at the Conference.

The Recommendations and their Application. A Review after Two Years. (4 Vols.)

World Economic Conference, Geneva, 1927:

Report and Proceedings of the Conference. Vol. I and Vol. II. (C.356.M.129.1927.II.) (C.E.I.46.)

International Monetary and Economic Conference, London, 1933:

Draft Annotated Agenda of the Conference, submitted by the Preparatory Commission of Experts. (C.48.M.18.1933.II.)

Reports Approved by the Conference on July 27th, 1933, and Resolutions Adopted by the Bureau and the Executive Committee. (C.435.M.220.1933.II.)

Agricultural Protectionism

Considerations on the Present Evolution of Agricultural Protectionism. (C.178.M.97.1935.II.B.)

Clearing Agreements

Enquiry into Clearing Agreements. (C.153.M.83.1935.II.B.)

Customs Administration

Studies on Commercial Policy and Customs Administration. (E.726.)

Vol. I: Methods of Application of Specific Tariffs.

Vol. II: Customs Treatment of Samples without Value; Customs Treatment of Printed Matter intended for use as Advertisements.

Dumping

Memorandum on Dumping, by Prof. Jacob Viner. (C.E.C.P.36.(1).) (1926.II.63.)

Memorandum on the Legislation of Different States for the Prevention of Dumping, with special Reference to Exchange Dumping, by Dr. E. Trendelenburg. (C.E.I.7.) (1926.II.66.)

Exchange Control

Report on Exchange Control. (C.232.M.131.1938.II.A.)

Marks of Origin

Economic Committee: Report to the Council on the Work of its Thirty-Fifth Session, 1931. Appendix III. (C.427.M.177.1931.II.B.)

Most-Favoured-Nation Clause

Equality of Treatment in the Present State of International Commercial Relations. The Most-Favoured-Nation Clause. (C.379.M.250.1936.II.B.)

Nutrition and Standards of Living

Final Report of the Mixed Committee of the League of Nations on the Relation of Nutrition to Health, Agriculture and Economic Policy. (A.13.1937.II.A.)

Preliminary Investigation into Measures of a National or International Character for Raising the Standard of Living, Memorandum prepared by Prof. N. F. Hall. (A.18.1938.II.B.)

Quotas

Quantitative Trade Controls: Their Causes and Nature. (1943.II.A.5.)

Raw Materials

Report of the Committee for the Study of the Problem of Raw Materials. (A.27.1937.II.B.)

Report on Certain Aspects of the Raw Materials Problems (with the relevant documents submitted to the Committee by Professor C. Gini). In 2 volumes. (C.51.M.18.1922.II.)

Tariffs

Special Memoranda and Reports:

Report of the Trade Barriers Committee of the International Chamber of Commerce. (C.E.I.5.) (1926.II.26.)

Commercial Treaties. Tariff Systems and Contractual Methods, by D. Serruys. (C.E.I.31.) (1927.II.26.)

Tariff Level Indices (followed by observations with reference to the methods employed). (C.E.I.37.) (1927.II.34.)

Stability of Customs Tariffs, by J. Brunet. (C.E.C.P.71(1).) (1927.II.17.)

Discriminatory Tariff Classifications, by W. T. Page. (C.E.C.P.96.) (1927.II.28.)

Economic Committee: Reports to the Council on the Work of its Thirtieth and Thirty-Third Sessions. (C.531.M.185.1929.II.) (C.641.M.260.1930.II.)

Tariff Systems and Contractual Methods

Recommendations of the Economic Committee relating to Tariff Policy and the Most-Favoured-Nation Clause. (E.805.) (1935.II.B.1.)

V. TRADE ANALYSES AND TRADE STATISTICS

The Network of World Trade. (1942.II.A.3.)

Europe's Trade. (1941.II.A.1.)

International Trade Statistics. (Latest edition. 1939.II.A.21.)

Balances of Payments. (Latest edition. 1939.II.A.20.)

International Trade in Certain Raw Materials and Foodstuffs by Countries of Origin and Consumption. (Latest edition. 1939.II.A.22.)

Raw Materials and Foodstuffs. Production by Countries, 1935 and 1938. (1939.II.A.24.)

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Monthly Bulletin of Statistics

Statistical Year Book of the League of Nations (1942/44 issue in the press).

World Economic Survey (1942/44 edition in the press).

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1. International Convention, 2. Protocol, 3. Final Act of the Conference. (C.606(1).M.184(1).1928.II.)

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