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Recovery

Program

UNITED KINGDOM
COUNTRY STUDY

Economic Cooperation Administration

February 1949 • Washington, D. C.

United Kingdom Country Study

European Recovery Program

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ERRATA SHEET

Page 4, line 27:

inflationary "pressures" instead of "measures."

Page 12, line 38:

Refers to a table which now appears on the following page. Correct the line to read "the table on the following page" instead of "the following table."

Page 33, line 12:

Delete "280," substitute "345."

Page 33, line 26:

Delete "only 92.6 import units in 1946 and 85.5 in 1947 and substitute "only 94.2 import units in 1946 and 92.7 in 1947."

Page 47, line 3:

Delete "million," substitute "billion."

Page 73:

Final paragraph, Section C on the Engineering Industries, first line of paragraph:

Delete "the table above" and substitute "the table on the following page."

Page 74, text line 8—Tanker Tonnage:

Delete "13.8" and substitute "3.8."

This document is based on the best information regarding the United Kingdom currently available to the Economic Cooperation Administration, and the views expressed herein are the considered judgment of the Administration. Both the text and the figures for 1949–50 are still preliminary in character; participating countries will therefore understand that this report cannot be used to support any request, either to the Organization for European Economic Cooperation or to the Economic Cooperation Administration, for aid in any particular amount for any country or for any particular purchase or payment.

Paul G Hoffman
Administrator.

FEBRUARY 14, 1949.

Contents

PART I

Summary and Conclusions

The United Kingdom requires economic assistance from the United States as a direct result of the damage of World War II. The basic recovery problem of the United Kingdom is to attain a balance in its overseas accounts at an acceptable domestic standard of living. This problem arises because of the loss of net income from invisibles and overseas investments liquidated as a result of the war; increased production is essential to its resolution. Since there is already full employment it will be necessary to rationalize and modernize production so as to increase output per man-hour. Another major aspect of Britain's long-term recovery is the problem of balancing its dollar accounts. Much progress has been made toward attainment of an over-all balance on current account, but to an important degree earnings in trade with other areas cannot be used to meet deficits in trade with the dollar area. The present outlook therefore requires Britain to stimulate its exports of goods and services to the Western Hemisphere in order to help balance its dollar accounts.

Important structural changes in the British economy are therefore necessary if it is to be successfully adapted to the conditions of the postwar world. British policy is designed to assist these changes by assuring that the country's resources are used in the first instance to increase exports and improve and expand productive capacity and only secondly to increase consumption. The British people have shown their understanding of the recovery problem by accepting the "austerity" which is one of the principal supports of the recovery program.

For 150 years, Britain was the main industrial workshop of the world as well as the chief center of world trade. Its growing population lived at a rising standard of consumption by the import of increasing amounts of foodstuffs and industrial raw materials and by the export of manufactured goods to the rest of the world. The pound sterling was the monetary unit in terms of which a large part of world commerce was carried on, and an important group of nations found it to their common advantage to tie their currency to the British pound and to maintain their monetary reserves in London.

Gradually, however, the United Kingdom, the first nation to be industrialized, felt the effects of competition, as parts of its industrial plant became obsolete and its exporters lost markets to the newer producers elsewhere in the world. These unfavorable trends were accelerated by World War I, during which Britain devoted its production to wartime needs and liquidated part of the overseas investments on which its standard of living depended.

Postwar recovery was slow but steady during the 1920's; the depression of the 1930's, however, further decreased earnings from overseas investments and made it increasingly difficult to market the products of British industry abroad. During this decade, the United Kingdom was already experiencing a small but persistent deficit in its balance of payments which might in fact have been substantially larger had the terms of trade not been more favorable to manufacturing countries than to nations producing raw materials.

The United Kingdom was unable to sustain the further drain imposed by World War II without liquidating a large portion of its overseas investments; the merchant marine suffered heavy damage from enemy action; capital plant was seriously impaired by bombing raids and continued undermaintenance and lack of repair. When the war was over, the United Kingdom faced a large deficit in its balance of payments despite the austere standard of living to which Britain had been reduced. The ability of the United Kingdom to become self-sustaining depends in large part upon the creation of sufficient new income on current-account to make up for the loss of overseas investments which have been liquidated.

Such a development depends upon an increase in both production and productivity within the United Kingdom and upon the maintenance of economy in imports. In general, this necessity is well understood by the government and people and notable progress has been made since the war in working toward these objectives. The United Kingdom hopes to move from a current deficit of 2.4 billion dollars on dollar account and a total gold and dollar drain of 4.1 billion dollars in 1947 to a manageably small deficit in its current dollar account and an estimated surplus of 400 million dollars in all currencies by 1952–53. Attainment of this goal will require a volume of exports 50 percent above 1938 and close to 40 percent above 1947, while imports will still remain below prewar levels. The output of manufactures in 1952–53 must be 40 percent greater than prewar and 25 percent greater than 1947 in order to sustain the projected level of exports and an acceptable domestic standard of living. World market conditions must be such as to permit the projected volume of exports to be sold.

These sizeable increases in manufacturing and exports require that large capital investments be made during the next 3 years not only in new production facilities but also in the modernization and improvement of existing plant and equipment, some of which was already obsolete before the war. Approximately 20 percent of the gross national product will be devoted to capital formation during each year of the program, principally in the basic fields of fuel and power, transportation, manufacturing of capital goods and industrial materials, and agriculture.

With such large portions of the national output reserved for export and for capital formation, and with imports restricted to levels below prewar, it is obvious that the resources remaining for the personal consumption of the British people are limited and will remain so until the recovery goals have been attained.

Since the critical year 1947, progress toward recovery has been steady. Production targets, which in 1948–49 average 125–130 percent of prewar, have already been met in most important industries. An outstanding success is the steel industry which exceeded its 1948 target by approximately 400,000 metric tons. The only exceptions have been coal-mining and the textile industry which, despite increased output over 1947, did not quite attain projected levels. As a result of this manufacturing effort and the limited domestic consumption, export volume increased in each quarter of 1948.

Although shortages of certain materials are still important factors limiting production, the major problem in attaining greater output is increased productivity. Since full employment has been reached, future production increases must in large measure come from additional output per man rather than from additional workers. Shifts in employment could assist in this effort, since certain essential industries, notably coal-mining and textiles, do in fact require a larger labor force and their failure to achieve the current year's targets is attributable in part to their inability to attract a sufficient number of additional workers.

For the past year the Government has attempted by various means to redirect labor to more essential employment, but with less than desired success. "Austerity" tends to limit the adequacy of direct incentives and despite the government's legal power to direct labor away from nonessential industries, some of these continue to absorb a larger share of the labor supply than originally planned.

Increasing out put per man-hour is essential to British recovery. Increases in productivity, however, are accomplished not only by capital investment; they are equally dependent on the effort put forth by labor and on the adoption by management of new and more efficient production methods. In the past 6 months both labor and management have shown a growing awareness of the need for better understanding and cooperation in eliminating antiquated and inefficient working techniques, labor practices, and methods of wage computation.

The physical limitations and difficulties faced by the United Kingdom in increasing productivity and production are accompanied by financial and monetary problems. Full employment creates relatively larger money incomes for most of the population but the necessity to further both the export drive and capital investment limits the consumer goods and services which these incomes can purchase. Inflationary pressures are therefore generated which fluctuate in degree as a result of various government policies. On the one hand, governmental expenditures are considerably larger than prewar, not only because of new burdens arising from the war but also because of some increased social service payments in the fields of health, education, and child and old-age care. On the other hand, subsidies are paid by the government to the producers and distributors of many essential consumer goods in an effort to keep down the cost of living and minimize demands for higher wages. Direct and indirect taxes are considerably higher than prewar; dividend payments are limited by voluntary agreement; the governmental budget anticipates a surplus for the current fiscal year. The government also maintains price controls, restrictions on nonessential investments, rations certain consumer goods, and allocates scarce materials to essential industries.

In addition, the government has used, with ECA approval, the sterling counterpart of ECA grant aid for retirement of short-term national debt. This has amounted to 82 million pounds, which is the sterling counterpart of 331 million dollars of assistance extended in the form of grants.

The net effect of these policies has been to control inflationary tendencies so that prices and tbe cost of living have risen only moderately during the past year. It is a tribute to the sense of national responsibility and the morale of the British people that these government controls are effective and that inflationary measures, though present in the economy, are prevented from having their full impact.

To contain and diminish inflationary forces, the government has therefore exercised an increasingly close supervision over the capital-investment sector of the economy by allocating available raw materials and equipment to essential capital projects and by attempting to prevent unnecessary investments. However, the prevalence of low interest rates and the easy credit situation may make it difficult to curtail nonessential investment to the extent desired.

During the current year, 1948–49, ECA aid has been an essential supplement to the efforts of the British people described above. Gross ECA aid of 1,239 million dollars for 1948–49 should permit a level of imports approximately 85 percent of prewar to be maintained. The heavy drain on British gold and dollar reserves which occurred before the start of the ERP has been checked, but ECA aid will probably not be sufficient to halt it completely. In comparative terms, however, loss of hard-currency resources this year will not be great. Reflecting increased domestic activity and rising exports, the rate of the over-all deficit on current account has been substantially reduced and the dollar position much improved.

The totals of the first two annual programs are summarized in the following table:

[In millions of dollars]

	1948–49	1949–50
United Kingdom request for gross dollar aid (budget basis)	1,271	940
OEEC recommendation of gross dollar aid	1,263	(1)
ECA estimate of gross dollar aid	1,239	940

[1] National submissions for 1949–50 not yet reviewed by the OEEC.

During the April–June quarter of 1948, the United Kingdom received an ECA allotment of 400 million dollars, 100 million dollars as a loan, and 300 million dollars as a direct grant.

For the fiscal year 1948–49, the total allotment proposed for the United Kingdom is 1,239 million dollars. Of this amount, a total of 919.1 million dollars has already been allotted and a further 319.9 million dollars remains to be allotted from the additional funds requested by ECA for the remainder of the current fiscal year. Of the amounts so far allotted for 1948–49, 213 million dollars is a loan, 232.3 million dollars conditional aid and 473.8 million dollars a direct grant.

Under the Intra-European Payments Plan, the United Kingdom is to make net drawing rights in sterling equal to 290 [1] million dollars available to the other participants to aid them in meeting estimated deficits with the whole sterling area. The net ECA aid to be received this year by the United Kingdom is, consequently, considerably less than the gross figure of 1,239 million dollars.

The second annual program, covering the period July 1, 1949, to June 30, 1950, projects further steady progress toward the objectives of 1952–53. The total volume of exports, projected at 145 percent of prewar, is to increase about 6 percent over projected levels for 1948–49. Total imports will remain at about the level projected for 1948–49. Production and exports will have to be sustained with a smaller proportion of imports than heretofore. Analysis of planned total imports as submitted to the OEEC indicates that the program is tight without leeway for further significant reductions if recovery goals are to be met and present modest consumption standards maintained. If the dollar outlay on food is to be kept to proposed levels, not only will United Kingdom home output have to meet planned targets, but availabilities for imports into Britain from areas other than the Western Hemisphere will have to meet estimated projections. If not, the pattern and dollar cost of the proposed import program may have to change.

[1] 8 million dollars to Turkey still subject to final approval by the OEEC.

Capital formation is expected to continue to consume about 20 percent of a somewhat expanded gross national product. Production is scheduled to rise to between 30 and 35 percent above prewar, or about 4 percent above 1948–49, and emphasis on production for the export markets will continue. Consumer living standards should improve therefore only in a very limited way, and then only if production has been increased enough to permit it.

In its submission to the OEEC for 1949–50, the United Kingdom estimated its need for ECA aid for the second program year at 940 million dollars, which is approximately three-quarters of the gross amount allocated by the ECA for the first program year. As the United Kingdom will undoubtedly make a substantial net extension of drawing rights to other participants during 1949–50, net ECA aid would be correspondingly less.

ECA's appraisal of the United Kingdom's need for aid during the second program year agrees in total with the British submission to the OEEC but differs in details, particularly in the composition of the import program.

United Kingdom recovery hinges primarily on its own production efforts in both industry and agriculture. The long-term program and the current export drive can succeed if Britain tackles the problem of productivity and costs objectively and with increasing energy. Coincident with the improvement in productivity, new and improved methods of marketing are required. Many weaknesses have already been remedied to a degree, but much remains to be done. Labor, management, and government in the United Kingdom now accept as a fact the need for increased productivity. The manner in which they are able jointly to attack this problem will decisively affect the future of Britain.

The export drive must be pushed with vigor, especially the increase of exports to hard-currency markets. Attention should be given to the design of new products, to packaging and marketing techniques, as well as to reductions in costs, if Western Hemisphere customers are to be won.

Although progress in each field of economic activity depends primarily upon British efforts, United States aid is required to provide essential dollar purchases, without which the progress of the British economy would be seriously impeded.

The British first and second annual programs are logical steps toward independence of extraordinary external aid. The substantial degree of progress already achieved by the United Kingdom, its generally sound fiscal policy, and the acceptance of austerity in its living standards offer assurance that aid extended to the United Kingdom will be effectively used.

PART II

Chapter I. Analysis of the Current Situation

INTRODUCTION

Consequences of the War

A Summary of Events Leading Up to the Current Situation

At the end of World War II, some of the major problems to be overcome by the United Kingdom were:

(*a*) Deterioration of industrial plant due to arrears of maintenance and obsolescence as well as general war damage;

(*b*) An excessive rate of drawings on gold and dollar reserves due to heavy postwar reliance on hard currency areas for needed imports;

(*c*) Increasingly adverse terms of trade, reversing the prewar pattern, making it more difficult to pay for imports with exports;

(*d*) Loss of net income formerly received on invisible account, from services and investment which in prewar years helped approach a balance on current account despite a traditional excess of merchandise imports over exports.

While the two world wars are responsible for these and other immediate difficulties facing the United Kingdom, other earlier developments, such as industrialization of new areas which became competitors, deprived Britain of its predominant place of the Nineteenth Century. In the United Kingdom prewar efforts to renew and improve techniques of industrial production lagged. Modernization of plant and even, in some instances, proper standards of maintenance were neglected.

In addition, there were changes in world demand patterns and British industry had only limited effectiveness in large-scale standardized mass production. These factors contributed to the steady deterioration of the balance-of-payments position which had become apparent even before World War II.

Before 1914, the United Kingdom's net income from current transactions was 900 million dollars a year and was reflected in large overseas investments. After 1925, net income was at the rate of 400 million dollars, but during the 1930's there was a net average deficit of some 100 million dollars a year, the rate in 1936–38 reaching more than 200 million dollars a year. While this deficit was not large in relation to Britain's total international transactions, it foreshadowed the wartime and postwar difficulties.

During World War II, the value of merchandise imports into the United Kingdom rose although the volume declined, and there were heavy government war expenses abroad. Income from abroad declined sharply as exports gave way to war production and the needs of the armed forces; by 1944 the volume of exports had fallen to less than one-third of 1938. Ship losses and increased needs for shipping precluded net earnings on shipping account and income from overseas investments declined due in part to liquidation of approximately 4.5 billion dollars of foreign assets.

With the end of the war, the United Kingdom faced the prospect of a continuing deficit in the balance of payments. The overseas deficit of 1.5 billion dollars in 1946 was financed by drawing on the United States and Canadian credits and by incurring additional sterling obligations. It was less than might have been expected, primarily because imports, impeded by world shortages, were slow to increase; wartime stocks of raw materials were drawn down, and there was rapid expansion of exports and increase in receipts on invisible account.

The improvement in 1946, however, concealed difficulties which reached crisis proportions in 1947. Accumulated stocks could no longer substitute for imports of raw materials. The early months of 1947 brought the worst weather in living memory, resulting in heavy livestock losses, a break-down of transport for several weeks, and interrupted industrial production. The shortage of fuel during most of the year was a serious handicap. World supply conditions required continued reliance on the dollar area and the rest of the Western Hemisphere for a large proportion of British imports. The dollar crisis became more acute throughout the world, and the continued rise in import prices increased the burden on the resources of the United Kingdom.

In accord with the Anglo-American Financial Agreement, the United Kingdom relaxed restrictions on the convertibility of currently acquired sterling on July 15, 1947. This contributed to a drain on United Kingdom gold and dollar reserves which, during July and August, ran at a rate in excess of 7 billion dollars per annum. On August 20, after conversations with the United States, the convertibility of sterling was temporarily suspended. At the same time the United Kingdom took drastic steps to improve its own balance-of-payments position and adjust its plans to current conditions. The

Western Hemisphere deficit for the year was 2.7 billion dollars and the total drain on gold and dollar resources was 4.1 billion dollars.

At the beginning of 1948 the central gold and dollar reserves of the United Kingdom were approximately 2 billion dollars. While these are the reserves of the United Kingdom, all countries of the sterling area, having traditionally held reserves in sterling, have had access to them. In its Economic Survey for 1948, the United Kingdom suggested that these reserves could not safely be allowed to fall much further, and that unless it could obtain aid under ERP it would be obilged to make further drastic cuts in imports from the Western Hemisphere.

An exact delineation of these cuts is impossible but their magnitude is indicated by a rough estimate made by the United Kingdom Board of Trade to explain to the British the effect of ERP allocations of aid on the economic welfare of the country. It was then calculated that rations of butter, sugar, cheese, and bacon would all have had to be cut by over a third, and there would have been even less meat and eggs than now. Cotton goods would have disappeared from the home market, supplies of footwear would have been reduced, and tobacco consumption would have been cut by three-quarters. Shortage of timber would have meant a further reduction in house building, perhaps to 50,000 units a year, or about one-fourth the present rate, and the electricity generating program would have been held up for lack of nonferrous metals. The supplies of raw materials for industry would have been even more seriously affected; the general dislocation of industrial activities would have resulted in increasing unemployment, perhaps up to 1½ million, and progressive deterioration could have been expected as the lower standard of living resulted in diminished productive effort. The results of ERP aid therefore are not so much to be seen in an improvement in the standard of living, but rather in the maintenance of the existing standard of living and in encouraging progress in production and exports.

Both industrial and agricultural production increased substantially in 1948, as did exports both to the Western Hemisphere and to the world at large. Imports were held to a level only slightly above 1947 and invisibles made a considerable recovery, returning a net income for the first time since the war. The drain on gold and dollar reserves was checked. The external deficit on current account with the Western Hemisphere has improved, having averaged for the first half of 1948 an annual rate of 1.57 billion dollars, which is little more than one-half of the 1947 deficit. In spite of less advantageous terms of trade, the annual rate of the over-all deficit incurred in the first half of 1948 was 1.4 billion dollars less than 1947. The second half year presents an even greater improvement over 1947.

Thus far ECA has issued procurement authorizations to the United

Kingdom in amounts which would have been sufficient to cover approximately three-quarters of its estimated lack of current resources to pay for Western Hemisphere goods. It is a reasonable conclusion, therefore, that without ECA aid in 1948 Britain would now be facing a crisis.

A. USE OF RESOURCES

1. An Outline of the Current Program

There are four general lines of action by which the United Kingdom hopes to attain economic viability and independence of extraordinary external aid: increased home production, saving in imports, expansion of exports, and development of overseas supplies. These are the main elements of the annual and long-term programs.

The United Kingdom program for 1948–49 proposes substantial increases in the level of production and exports in comparison with 1947, but more limited goals in relation to levels already achieved during the first half of 1948. Imports will rise modestly but the shift in the direction of demand away from hard currency areas will be more marked. Domestic consumption will remain approximately at current levels, and investment will absorb 20 percent of the gross national product.

The United Kingdom itself has not published an official statement of the current status of its national accounts, but from progress to date toward targets in the major industrial sectors, it is estimated there will be an increase of approximately 2 or 3 percent in gross national product in the United Kingdom during 1948–49 as compared with the level of output at the beginning of the period. During this period it is estimated that the United Kingdom will incur a deficit on current overseas account equivalent to less than three-quarters of a billion dollars. The total of resources available for use at home will be approximately 42 or 43 billion dollars. For 1947, the comparable figure is 41 billion dollars, including resources made available by incurring an overseas deficit of 2.5 billion dollars.

The United Kingdom has announced that it will devote 20 percent of this gross national product to investment and gives this value as approximately 8.0 billion dollars. The Government share on defense account is not yet slated to increase to any disturbing degree, and personal consumption, reflecting continuation of the present policy of austerity, is expected to be at levels roughly equivalent to those of today.

Although the targets described in the United Kingdom submission all represent appreciable gains when compared with 1947, they represent modest advances over the levels already attained by July 1, 1948, the start of the new program year. Thus, coal production is to increase by 1 or 2 percent over January–June 1948; and manufacturing activity has a possible range of increase of 2 to 5 percent. A similar comparison for agriculture is not possible, but production in the 1948–49 crop year is expected to exceed 1947–48 approximately by 9 percent. While some other components of economic activity closely related to the manufacturing activities will show corresponding increases, the large segments of the economy comprised by government, personal and professional services, finance, etc., are unlikely to show any substantial increases because of manpower stringencies and the effort to direct labor into other activities.

The gross national product in the United Kingdom had attained in the early part of 1948 an annual rate of approximately 40 billion dollars. An increase in gross national product of 2 to 3 percent, without any price changes, would amount to 750 million to 1.3 billion dollars, and such an increase, applied to specific sectors of the economy, could have considerable significance.

In preparing forecasts for 1948–49, United Kingdom planning officials undoubtedly considered the possibility of marginal increases in total availabilities of resources and the probable areas of use.

If further defense expenditures do not materialize, and if production does rise in the magnitude estimated, it may be possible to increase exports and consequently imports above the suggested levels. There may also then be a larger supply of domestic products. The task of modernizing United Kingdom industry could profitably absorb much greater resources if available. Any domestic production still available after increasing the rate of investment can be used to raise consumption of such items as textiles and consumer durable goods as well as to step up the construction program. In view of the low levels of consumption still prevalent in these sectors, even small increases would be beneficial.

2. Consumption

The word "austerity" has become synonymous with British self-discipline and determination to achieve recovery. During and since the war the British have denied themselves important elements of their traditional standard of life. The Government, following its stated policy that consumption must take second place to the country's needs for new plant and equipment and for exports, has employed a combination of measures which in scope and effectiveness are almost without peacetime precedent in a democratic country. Fiscal policy limits home consumption by high taxation, thus assisting to channel a large part of British production into investment and exports. Import controls restrict expenditures abroad and thereby conserve foreign exchange. Rationing and other policies successfully employed in the distribution of consumer goods have not only contributed to the effective support of the austerity program but have permitted essential needs to be met with a smaller supply of goods than would otherwise have been required. Allocations of scarce materials have also been used to limit production of goods for home consumption and expand production for export.

During the present program year (1948–49) consumption in the United Kingdom will be maintained at about the same general level as in the preceding year. However, owing to the continuance of restrictions imposed after the financial crisis of 1947, there will be less of certain manufactured goods than in 1947.

Household goods have generally continued to be scarce and are rationed items. A hoped-for increase in textile production has been slow of realization and home supplies of some types of cloth important to export markets are shorter than in 1947. Beginning in February 1949, however, there was a relaxation in clothes rationing. Footwear had also been released from rationing and rising production of household goods is expected to result in an increased supply for the home market.

Although the caloric levels of food consumption in the United Kingdom during 1948 were adequate, the quality of the diet deteriorated still further, with decreased meat consumption being offset by higher consumption of other foods such as cereals and potatoes. Meat imports during the first 10 months of 1948 were only 78 percent of the volume of arrivals during the same period in 1947 and arrivals were lagging behind expectation.

Though rationing will continue, food consumption in the United Kingdom, it is hoped, will show a slight improvement by the end of the 1948–49 period. Food consumption per man per day will probably average close to 2,900 calories, compared with 2,825 calories in 1947–48 and 2,950 in the prewar years. A comparable average per capita consumption in the United States is approximately 3,250 calories.

The increase in the calorie level in 1948–49 over the previous year is for the most part due to the increased supplies of cereals and potatoes. Milk consumption has increased but consumption of meat, fats, eggs and sugar will remain substantially below prewar. With increasing supplies of fruit and vegetables, however, the adequate but unvaried diet should lose some of the monotony it has had since the war. The following table compares the estimate for 1948–49 with the pattern of the past.

Food supplies are still limited and rationing is necessary to obtain equitable distribution, although with high employment and better distribution, nutritional levels have improved over prewar for many people, particularly in the lower-income groups. The severity of the situation may be illustrated by the continued necessity for close rationing, as follows:

Estimated per capita food consumption in kilograms per year in the United Kingdom

	Prewar	1947–48	1948–49 (preliminary)
Grain as flour	95	115	119
Sugar (refined) including glucose in terms of sugar	49	37	38
Potatoes	79	111	130
Pulses	3	2	3
Vegetables	55	56	63
Fruits and nuts	60	46	54
Meat (Carcass weight)	65	48	44
Fish	24	28	35
Eggs	11	10	9
Whole milk	126	156	153
Cheese	4	4	3
Fats (fat content)	21	17	18
	Calories per person per day		
Total	2,950	2,825	2,900

The weekly meat ration is 1 shilling's worth [2] and is currently threatened by lagging shipments on existing meat contracts. The Ministry of Food announced that after January 23, 1949, the fresh-meat ration would be reduced. The bacon ration remains 2 ounces, with the hope that it may be increased to 3 ounces for a short period before the close of this program year. In November 1948, occasioned by a short-fall of 10,000 tons in the flow of supplies, there was a cut in the bacon ration, stretching the ration to last a fortnight instead of a week. Restoration of the ration was announced for January 30, 1949.

The weekly cheese ration is now 1½ ounces. Bread, cereals, and potatoes are off the ration. In December 1948, the weekly sugar ration was increased from 8 to 10 ounces and the weekly candy ration from 3 to 4 ounces. The cooking fats ration was raised from 1 to 2 ounces for a period of 16 weeks, and it has been possible to deration jams and marmalade. The tea ration, however, has remained at 2 ounces a week, disappointing hopes for an increase to 5 ounces a fortnight.

According to present tobacco programs, per capita consumption is expected to drop from 2.5 kilograms in 1947–48 to 2.3 kilograms in 1948–49, roughly a decrease of 8 percent. Tobacco consumption in 1948–49 on a per capita basis, it is estimated, will average almost 10 percent higher than prewar, despite the very high taxes smokers must pay. The number of smokers has also increased greatly.

Food subsidies have kept the prices of bread, potatoes, milk, fats, sugar, meat, bacon, cheese, eggs, and tea within the reach of all, and contributed to the equitable distribution of short food supplies. Subsidies have been applied against imports, so that the price to the consumer is considerably cheaper than the import cost. In the case of domestically produced foods, subsidies have taken the form of guar-

[2] 20 cents.

anteed prices to farmers, including acreage payments. These also have anti-inflationary effects, since processors' and distributors' charges, usually on the percentage of cost basis, are kept to a minimum.

Housing requirements have reflected not only the war losses but also arrears in repairs and maintenance, normal depreciation, the changing pattern of industry, and the fact that the population has increased since 1939 by more than 2¼ million. Housing continues to yield priority to more essential needs in the economy, but wartime damage and destruction, which made more than 470,000 houses uninhabitable, has now been recovered. Between the end of the war and midsummer 1948, the United Kingdom built 330,000 permanent houses, 155,000 temporary houses, and restored to use through conversion or repair an additional 235,000 units. The current rate of construction, about 200,000 houses per year, is expected to continue and it is expected preference will be given to construction that will facilitate recruitment of workers in undermanned industries and in those where substantial expansion is expected. So far as the average consumer is concerned, there is no present hope for the replacement of obsolete units or those which did not meet even prewar standards.

It is evident that since the economic crisis of 1947 the United Kingdom has recognized that resources are insufficient to support the ambitious plans originally contemplated in 1945 and 1946, and has reduced and deferred these programs accordingly.

The United Kingdom had planned in its Economic Survey for 1948 for a shrinkage in the labor force in the distributive and service trades which has not materialzed. Actually there were increases, and if these gains are not reversed, the consumer may enjoy a somewhat better level of services during 1948–49.

3. Capital Investment

(*a*) *Magnitude of investment.*—Britain lost nearly 5 billion dollars worth of domestic capital assets as a result of the war. Bomb damage to buildings, equipment, machinery, and transport accounts for 2.2 billion dollars of this total. An even greater loss came through "disinvestment"—the reduction in value due to inability to repair and maintain physical equipment. Damage to the railroads from both causes was particularly serious and resulted in internal difficulties which hampered distribution and recovery efforts in the two years immediately following the war.

Total war loss of capital was equivalent to almost seven times the amount of new capital added to Britain's physical resources in 1938.

The outstanding feature of capital investment in the United Kingdom in 1948 is the fact that through exceptional effort a good deal more has been accomplished than was thought possible or planned. In September 1947, following the dollar crisis, the Government reduced the investment program for 1948 by over 10 percent and aimed at even sharper cuts in the rate of investment to stay within tightening supplies of critical materials such as steel and timber and to avoid possible interference with the export program.

Latest estimates of fixed capital formation are 7.6 billion dollars for 1947 and 8.0 billion dollars for 1948, indicating that this reduction did not occur. The substantial increase in national production over the levels of July–September 1947 and the Government fiscal policy, intended to restrain and diminish inflationary pressure, were important factors permitting increased capital formation. The volume of exports was less during the first half of 1948 than anticipated in early planning, but steel production exceeded expectations and more materials were available for housing, allowing improved rates of completion. At the same time, continuation of restraints on consumption and controlled Government expenditures have allowed the rate of exports to increase without disturbance to the balance of inflationary forces at home. Official recognition has been given to the fact that total domestic capital formation (including inventory accumulation) is proceeding at the original gross rate of over 8.2 billion dollars and it may even be considerably greater. Unofficial estimates indicate a gross rate of 8.6 billion dollars for 1948.

In physical terms, these developments in the capital investment program can be regarded as an important contribution to the solution of Britain's problem of modernizing its economy to enable it to compete effectively in world markets and progressively increase its standard of living. To attain this objective, the British must overcome not only the wartime destruction of fixed assets and forced postponement of regular maintenance and repair, but arrears of a long period preceding the war when the level of investment in industry was insufficient to maintain competitive levels of efficiency and overcome the inroads of obsolescence.

Against this background, recent progress in capital accumulation is quite modest. By the beginning of 1948 approximately the losses and wear of the war had been made good, but there still remained the increased population to be housed and to be provided with working tools. A certain imbalance in the pattern of capital formation also remained to be corrected. Many old industries were worn down and inefficient, as the war had demanded that investment flow into new industries in the machinery and chemical fields.

Today, with a gross national product of about 40 billion dollars or slightly more per year, the planned gross investment of about 8.0 billion dollars represents, as previously stated, an allocation of 20 percent of the national product to investment. Direct comparison with higher rates of investment in the United States is of questionable value because the degree of effort they represent is relative to the differing levels of the two economies and what they can afford. There is, however, fairly general agreement that a further effort to increase aggregate capital formation is required to accomplish the necessary modernization of the United Kingdom productive machine.

(b) *The pattern of investment.*—Up to this point capital formation has been considered only in gross and aggregate terms. About half of gross investment, estimated at 4.0 billion dollars in 1948–49, is required to cover the depreciation of capital assets. Only the balance, or net investment, is available for the expansion of productive capital as well as to make up wartime damage and arrears of replacement and to provide housing for the increased population. Net investment, therefore, is a better indicator of the probable length of time required to accomplish the capital development programs.

Vital as schools, housing, and hospitals may be to national well-being and to a permanent improvement in the level of production, it is the industrial sector which must support Britain's competitive position in world markets.

A recent study of industrial reequipment in the United Kingdom [8] which may be used as a guide to the real position, suggests that gross expenditures on fixed capital in productive enterprise (excluding housing, schools, and public buildings) was about 20 percent below 1938 in 1946, 10 percent higher in 1947 and probably 15 percent higher in 1948. On the net basis which determines the forward strides in industry, after allowances are made for depreciation, replacement, and war damage, there was no gain in 1946 and 1947. The study concludes that in 1948 net investment in industry will approximate 800 million dollars which is much less than in 1938. Without accepting the exact figures of the study, the calculation of magnitudes and proportions may still be used to suggest the extremely limited volume of investment that has so far been available to do more than merely restore industrial losses.

A further qualification suggested is that aside from necessary war damage, repair and housing, capital investment to date reflects a certain concentration on new factory building in the development areas with the purposes of diversifying industry and promoting long-run employment stability. At the present time, emphasis is also on big projects in basic industries—electricity, steel, coal, petroleum and chemicals—which will absorb a large proportion of investment resources and, because of their size will take longer to mature than smaller projects in some of the intermediate processing and finishing industries. Without touching on the social policies involved, this concentration of effort on some of the basic elements of industrial production does not appear to be an unreasonable approach to the United Kingdom's real problem of industrial balance.

[8] Reequipment of industry. Times, London, Oct. 15 and 16, 1948.

Increased home capacity of this type can both reduce dependence on external supplies and raise export earnings on a value added basis. Furthermore, a permanently expanded level of production will require a higher degree of support from these basic trades. The United Kingdom has at the present time a high finishing capacity in the key trades relative to its basic industry, but this sector also needs improved levels of efficiency. The United Kingdom drive must be selective and direct the limited capital resources into those sectors most urgently in need of modernization and expansion and which have the closest immediate bearing on raising national output, efficiency, and export capacity.

The pattern of investment as evidenced by construction trends to date shows increased emphasis on industrial and agricultural capital formation and away from the less directly productive capital such as housing. The value of work done on new houses reached its peak at the end of 1946. Industrial and agricultural projects have risen from 13.9 percent of total construction in 1946 to 19.2 percent in the second quarter of 1948, while all nonhousing has risen from 33.6 percent in 1946 to a rate of 44.1 percent of total construction.[4] Indications are that home supplies of major types of producers equipment have also increased substantially over 1947, and are probably accounting for a steadily increasing share of gross domestic capital formation.[5]

In describing the long-term program, the United Kingdom indicated that an annual average of about 56 percent of the investment program is to be allocated to the basic industries—fuel and power, transport, communications, agriculture, and manufacturing. In 1948–49, investment in the coal industry will take about 100 million dollars for a combination of short- and long-term projects. About 520 million dollars is programed for the first stage of the electric-power program. The program for investment in oil refinery construction can only be appraised as a part of the long-term program and the production stage is still in the future. Investment in the steel industry during the current fiscal year is scheduled to consume 160 million dollars as part of the long-term drive to increase steel capacity. Investment in maintenance and repair will absorb the most substantial part of total investment in the machinery and vehicle industries which are vital to increased production and export. While there will be a major expansion of facilities in the chemical industry started with the 1948–49 program, these projects will for the most part come into production only later in the recovery program.

In some of the older industries, such as textiles and pottery, the

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[4] Source: Compiled from London & Cambridge Economic Service Bulletin, Nov. 18, 1948, p. 135.

[5] Ibid., p. 136.

investment program will be directed to modernization of plant and equipment and the improvement of factory conditions in order to increase production and productivity and to lower costs and attract and hold labor. Since the transport system has not entirely overcome wartime arrears in repair and maintenance this will be a prime charge on investment during 1948–49. Rehabilitation of the merchant marine has been moving rapidly forward and it now seems probable that by the end of 1948, 1.2 million gross tons of vessels will have been produced.

Between 5 and 6 percent of the available investment resources valued at approximately 400 million dollars are expected to be devoted to both physical improvement of agricultural plant and to improving agricultural methods and techniques during the current year.

An increase in the industrial investment program would have to come from either greater than planned production or out of the programs now planned for housing, water supplies, health, education, other public administration, and present provisions for rearmament.

Current investment in roads, schools, water supply, sewers, and hospitals makes only a relatively modest demand on physical resources. The volume of expenditures in 1948 is substantially below prewar levels and will be devoted largely to overcoming arrears of maintenance and making essential replacements. New construction would thus be limited to facilities required for public health and safety or to improve collateral services furthering production and industrial efficiency.

In view of the possible necessity for an expansion in the defense program, the allowance for this item may be inadequate and other segments of the investment program may have to be reduced to accommodate it.

It is questionable that any substantial diversion from the nonindustrial sector is either desirable or feasible. The investment programs in housing, health and education have already been trimmed substantially from levels projected in 1947. Housing, which represents the largest part of this segment, is mainly concentrated in those industrial areas where lack of acommodation is preventing the expansion of production.

A housing program which calls for a steady output of about 200,000 houses per year covers obsolescence and depletion on Britain's stock of 12 million houses, but does not allow for improvement of housing standards or needed housing for population increases.

The educational investment program emphasizes the provision of facilities for technical training. Other major needs have not yet been met and the general reform to raise the school-leaving age to 16 years has had to be deferred for lack of adequate school buildings.

4. Exports

The United Kingdom program for 1948–49 suggests an average volume of exports from domestic production at 137 percent of 1938. The average for 1947 was 109.

Actual export volume[6] during the third quarter of 1948 was above the estimate for 1948–49 and averaged 138 percent of 1938, rising from an average of 126 and 134 in the first and second quarters, respectively. Additional gains, for the fourth quarter, resulted in estimated volume of approximately 147 percent of 1938. If these rates can be maintained, increases over the program level suggested for the year could certainly be expected. The major problems of production in appropriate volume and quality necessary to support the export program and meet price competition must be met. In addition, difficulties posed by existing import restrictions in other countries, and similar problems must be overcome.

In building up export totals in 1948–49 the major role will be taken by the capital equipment and vehicles industries, which together are expected to provide more than one-third of export values. Textile materials and manufactures are the second most important category and are expected to supply approximately one-fifth of export values. Exports of machinery and vehicles have already exceeded monthly target values for the end of 1948. Textiles and textile manufactures lagged somewhat.

United Kingdom export plans for 1948–49 call for an increase of 45 percent over 1947 in volume of exports to the Western Hemisphere, where the balance of payments problem is the most serious. These markets in the Western Hemisphere were expected to take 16.5 percent of total exports.

Since the possibility of total exports higher than programed has been indicated, the question arises whether the United Kingdom can increase hard currency earnings on visible trade above the levels suggested in the 1948–49 program. Analysis of the program in the light of recent experience indicates that although there may be some differences of destination, it does not seem likely on over-all account that the estimate of dollar earnings will be very significantly exceeded. Exports to other participating countries, to the dependent overseas territories, and to the rest of the world are also expected to rise substantially over 1947.

On invisible account in 1947 payments exceeded receipts on total account by more than 700 million dollars. Although on Western Hemisphere dollar account there was a deficit close to 600 million dollars,

[6] A caution should be extended against accepting the Index of Export Volume, quoted here, as an absolute indicator of the volume of exports Due to the technique employed in construction of the index it may under present conditions overstate actual volume.

there was a surplus on Western Hemisphere nondollar account of less than 100 million dollars.

This serious deficit position in invisibles improved markedly during the first half of 1948, largely because of a reduction in Government expenditures overseas, particularly on military, relief and rehabilitation, and occupation account. A surplus on total invisible account equivalent to an annual rate of 128 million dollars was realized. Despite the general improvement, however, accounts with the Western Hemisphere indicated an annual rate of deficit of 146 million dollars on invisible account. Much of the improvement in the Western Hemisphere account can be attributed to elimination of dollar procurement for civilian consumption in Germany.

For 1948–49 the United Kingdom projected a net surplus on total invisible account somewhat higher than that realized during the first half of 1948, and a reduction in the deficit on Western Hemisphere account, especially by improved receipts in the nondollar areas. Final data for calendar 1948 are not yet available but there are indications that the estimate for 1948–49 may also be exceeded.

B. SOURCES OF RESOURCES

The British economy is supported by intensive domestic production in both industry and agriculture and by a flow of supplies from abroad without which existing levels of activity and consumption would be impossible.

1. Production

(*a*) *General.*—The United Kingdom program for 1948–49 sets production goals which, as shown in the table below, are high compared with prewar and still substantial compared with 1947.

United Kingdom production goals proposed for 1948–49

	Index prewar=100	Index 1947=100
Manufacturing	125–130	115–120
Agriculture	130	108

These levels appear to be already substantially attained by activity during 1948. Manufacturing during the first six months of 1948 was 25 percent above prewar, despite monthly fluctuations. The table below gives recent production trends in greater detail.

Interim index of industrial production

[Index number based on 1946=100]

	1935-38	1946	1947	1948 First quarter	1948 Second quarter	1948 Third quarter	Average for 3 quarters 1948	October 1948 (preliminary)
Total, all industries	101	100	108	120	122	115	119 0	127
Manufacturing	98	100	109	122	124	118	121.3	128
Mining and quarrying	127	100	102	111	111	101	107.7	116
Building and contracting	137	100	111	116	127	121	121.3	136
Gas, water, electricity	66	100	103	119	102	95	105.3	111

There are a number of factors which point to the possibility of greater activity in 1948–49 than is contemplated in the estimate given above. Unofficial British estimates suggest that productivity in most industries has recovered to the prewar level. In 1948–49, the replacement, restoration and recovery which have already occurred may effect some additional increases in productivity. However, there will be few net additional workers as a result of reduced releases from the armed services.

(*b*) *Distribution of labor force.*—The Government has been trying for about a year to improve the distribution of labor. Several policies have been directed to this purpose:

(1) The controls over capital investment, raw materials, building licenses, etc., basically designed for the most effective use of raw materials and limitation of demand to curb inflationary tendencies, will have some effect in reducing opportunities for employment in the less vital sectors of industry, releasing labor for more essential work.

(2) Unemployed workers are not permitted to take jobs except through the public employment offices established in October 1947, which try to persuade them to take employment in industries on the preferential list for labor. Compulsory powers are rarely used but are held in reserve.

(3) Essential undermanned industries have priority for housing.

(4) Since February 1948, the Government has tended to discourage wage claims in the less essential industries, but takes a more sympathetic view of wage increases or other improvements in the essential undermanned industries.

This combination of policies has effected the following shifts: Between December 1947, and August 1948, 41,000 workers were added in essential manufacturing and 10,000 in other essential employments; this was an increase for both groups taken together of only slightly more than 2 percent.

The Government's efforts to cut down the force in the less essential industries have been less successful. About 11,000 were shifted out of less essential manufacturing, but in other less essential employments there was an increase of nearly 64,000. Instead of getting a decrease in the numbers employed in all work classed as less essential, there was, therefore, an increase of about one-half of one percent.

The Government has also tried to recruit foreign workers. In 1948, more than 100,000 foreign workers entered the United Kingdom under International Refugee Organization and Government projects, and on individual work permits. Additional projects to bring in needed female textile workers are being planned.

None of the industries important to British recovery are seriously handicapped for want of labor except coal and textiles. Efforts to expand manpower in the vital industrial sectors have met with considerable success in the case of transport, shipping, metals, engineering, and agriculture. The hoped-for expansion in the coal and textile industries, however, has been disappointing.

c. Fuel and power availabilities—Coal.—Coal is a major source of indigenous wealth in material resources in the United Kingdom. Home supplies of other fuels are insignificant. Traditionally it has also exported a substantial proportion of coal production, as high as 20 percent in prewar years, in combined overseas shipment and bunkers. Coal output has not yet recovered to prewar levels but considerable progress has been achieved.

Production in 1947 totaled 200 million metric tons as compared with a prewar average of 233 million metric tons. The target for 1948 was 214 million metric tons (211 million long tons) of combined deep-mined and open-cast production. Actual production failed to make the target by 2.5 million metric tons. The 1948–49 program calls for a further increase in production to a target of 218 million metric tons. Thus far the mines have not succeeded in approaching these levels and production is at an annual rate of approximately 215 million metric tons.

Mining has been designated a first priority industry for additional manpower. Targets called for a total of 750,000 workers on the colliery books by the end of 1948; pay rolls are approximately 25,000 workers below this target.

Productivity in coal mining has improved substantially; output per man-shift is approaching but has not quite reached the prewar average of about 1.16 or 1.17 long tons. Reported output per man-shift in June 1948, was 1.11 but midsummer holiday season resulted in some fall from this level to 1.07 in July and 1.08 in August. By November 1948, the weekly average output per man-shift worked had risen to 1.15; output per man-shift worked at the coal face was equivalent to prewar.

The program for 1948–49 and the long-term program are parts of an over-all plan for the coal industry, the complete realization of which may take some 10 or 15 years. In 1948–49 this over-all reconstruction program will be in its early stages and about 100 million dollars will be devoted to replacement of equipment, coal preparation plant, redevelopment of existing pits, sinking of new pits, and projects to increase output or reduce costs by mechanization and reorganization. All these represent combinations of both short- and long-term investment projects, and at the early stages the contribution to production and productivity in 1948–49 of even the short-term projects will be difficult to measure.

The National Coal Board is attempting to concentrate production in the most efficient mines, and the real question is whether the Board can reduce costs before market conditions force the issue. In the immediate future any prospect of lower costs lies in a consolidation of effort in the most productive areas and in increasing productivity.

There also is a drive toward a greater efficiency in coal combustion and since the end of the war, industrial users have made some adjustments to enable them to use lower grades of coal.

Petroleum.—Supplementing expanded coal production the United Kingdom hopes for increased availability of petroleum products during 1948–49 through increased imports.

The United Kingdom is not only the world's third largest consumer of petroleum products, after the United States and the U. S. S. R., she is also, through British controlled companies, the second biggest producer of oil, despite the fact that only a negligible quantity of crude is found on British soil.

British and American companies have large-scale development projects under way in an effort to increase Middle East production as quickly as possible, and it is hoped Europe will receive the major portion of its supplies from these areas instead of from the Western Hemisphere. Meantime, British oil companies with producing fields in the Caribbean area may be able to earn additional dollars for Britain by increasing their sales to dollar countries.

To handle Middle East production, refinery capacity will have to be increased in western Europe and the Middle East; the United Kingdom plans approximately a four-fold increase in domestic refinery capacity by the end of 1952–53. This will still be less than total domestic consumption requirements, and exports except for specialty products, will be limited.

Electricity.—Electric power output during the first 10 months of 1948 was approximately at the rate suggested in the 1948–49 program.

Approximately 130 million dollars is being programed for investment in the electric power industry during 1948–49, as a start on plans to overcome the tight situation in electric power supply which is straining present capacity.

The present electric power shortage, which constitutes a major limitation on expanding production, is due to wartime arrears of maintenance and limitations on expansion, and to an increase of approximately 80 percent in power demands as compared with 1938. Present generating capacity which cannot meet winter peak-load requirements must be raised about 40 to 50 percent.

By resorting to a number of devices to reduce the peak loads, especially during the winter months, a 20 percent reduction in industrial peak-load demand was accomplished in the winter of 1947–48 and a similar goal has been set for the winter of 1948–49. Street, shop, and restaurant lighting is limited, display and advertisement lighting prohibited, and new requirements for commercial, farm, and domestic power are met only when a case can be made for their essentiality. Expansion of the gas utility industry will also help somewhat to keep down electricity requirements.

The program for electric power expansion faces a number of serious problems including a severe shortage of wood poles for line extension, the scarcity of steel for generating equipment and buildings, and the cost and quality of coal supplies.

The United Kingdom has reduced the original electric power expansion program submitted to OEEC to maintain heavy exports of approximately one-third of its production of electric power-generating equipment.

The nationalization of the electric utility industry has not interfered with current present output, nor the expansion plans. About half the industry was already publicly owned and all operations were under close public utility control, so that the transition to nationalization involved no drastic readjustment.

While the combination of increased coal production, better availability of fuel oil and electric power output approximately 5 to 6 percent greater than in 1947, probably should be sufficient to support the proposed level of industry, it should be remembered that the British have reached their coal export targets for 1948 by drawing on coal stocks to make up the short fall in production and will probably continue to favor exports at the expense of domestic use.

d. Steel industry.—The United Kingdom's postwar plans visualized an expansion in the steel industry to assure 16 million tons crude steel capacity as soon as possible. This was an increase of approximately 2 million tons over estimated capacity in 1938. Since that time it has been recognized that export objectives depend even more on products made largely of steel than originally expected and claims of other expansion programs have also increased. It is now estimated that for a permanently higher level of industry, requirements may be more than 18 million tons in the early 1950's. The industry has estimated that by a combination of improved methods and techniques, retention of some plant intended for displacement and higher limits of capacity in the detailed schemes than in the broad estimates, this will be possible.

Good management, careful planning and additional development programs will be required to assure the necessary supplies of fuel and raw materials to allow such levels of production.

By 1952, the United Kingdom plans for crude steel output of 17 million ingot tons. Even so, steel availabilities will continue to be a limiting factor for production and investment throughout the ERP period, and even in 1952–53 imports will be required to meet the total demand. The effect of any further expansion of the defense program at this point may be decisive.

In 1938, the United Kingdom produced 10.5 million metric tons of crude and semifinished steel. This was considerably less than the 13.2 million tons produced in 1937, the most active prewar year, but both are below present levels of activity, which have been exceeding targets.

For 1948–49, the United Kingdom program suggests a crude output level of 15 million ingot tons (metric). This is approximately 300,000 tons more than the target for 1948, which was revised in July because of the record achievements of the second quarter. Weekly average production during the second quarter of 1948 was equivalent to an annual rate of 15.6 million metric tons. The annual rate for the first 11 months of 1948 was 15.2 million metric tons and production in November actually attained a rate of 16.0 million metric tons. Although output in December declined as it usually does, it was the highest of record for December. Total output for 1948 was 15.1 million metric tons, 400,000 metric tons over the target for the year and higher than the original target for the 1948–49 program. This achievement was aided by agreements between labor and management to undertake 7-day continuous operation; by the increased efficiency of oil firing, and the coming into production of some plant expansions. If the necessary flow of supplies can be maintained, it is believed crude steel production will exceed the target of 15 million tons for 1948–49. The British had in fact counted on such an excess for 1948. In comparison with earlier periods, however, the increased production must in part make up for reduced imports of ingots and semifinished steel.

The finished steel production target of 11.6 million tons for 1948–49 also has good prospects of realization in view of increased domestic production and increased supplies from Belgium, secured through use of drawing rights and hard currency settlements.

Increased steel production can be regarded as favorable to the present progress of the economy since want of steel has been an important limitation on production, modernization, and rehabilitation plans. If higher levels of production than projected in the original program draft are realized, it may also mean an increase in total exports since machinery and metal goods contributed 48 percent of the total value of exports out of domestic production during the first 9 months of 1948.

A bill to nationalize the iron and steel industry is now under consideration by Parliament. For parliamentary reasons, final action on the measure may be delayed until late 1949 or early 1950.

e. Textile industry.—The textile trades have been able to contribute substantially to the export program despite the failure in some lines to reach established targets. Prewar, the industry was affected by a decline of approximately 80 percent in cotton exports, paralleled by a decrease in capacity which reduced looms and spindles in operation by approximately 50 percent. Postwar activity has increased and consumption of raw cotton, though 30 percent below 1935–38, was 17 percent above the 1946 rate by October 1948. Recent revision of export targets has given cotton the greater share of the increase for the end of 1949.

Recruitment of additional textile workers has lagged and there is great necessity for increasing productivity through increased mechanization and improved working methods. On the showing of the present program the planned addition of textile machinery does not seem to be entirely adequate for this purpose. This is in part due to slow deliveries from abroad and in part to the delayed acceptance of the necessity for modernization and improvement by textile manufacturers. However, the Cotton Board is sponsoring efforts to increase production and productivity through redeployment, improved managerial efficiency, revision of obsolete wage systems, modernization of machinery, reequipment and improvement of structures. In the woolen and worsted industries reliance is placed on the individual firms to promote the improvements needed.

Existing equipment in the wool industry is not in much better condition than that in the cotton industry, for the industry is also an old one. Activity, however, has increased and raw wool consumption during the third quarter of 1948 was close to 30 percent greater than in 1946, and slightly above 1935–38.

The synthetic fiber industries are in the best position in terms of capital equipment since they are the newest industry.

Employment in the textile industries as a whole showed a net gain of 34,000 persons during the first 10 months of the year, but net recruitment has fallen well below expectations, and at the year end may still be approximately 70,000 workers under the target. As indicated, further attempts to recruit foreign textile workers are planned.

f. Machinery and equipment industries.—In the engineering industries which produce a variety of manufactured goods including machinery, vehicles, electrical goods, and assorted metal manufactures, implements, and instruments, production has increased rapidly and second quarter 1948 operations were at a level 55 percent greater than 1938. Exports in these categories of goods have been notably successful and for the first half of 1948 provided about 37 percent of United Kingdom exports as compared with about 25 percent in 1938. This volume of export leaves about two-thirds of engineering products for domestic use, largely in the capital investment program.

The most important labor requirement to be met for these industries is for qualified technical people in a few significant categories, such as production engineers and tool designers. A major factor in contributing to the industry's achievement during the first half of 1948 was the improved flow of supplies, especially of steel, which enabled the existing labor force and capital resources to be employed more effectively.

The British machinery and engineering industries are organized in small units where acceptance of new equipment and techniques may be slow, but in general the industries are regarded as well equipped and well managed.

Export targets of double 1938 volume or better had been set for the industry for the end of 1948 and may well have been realized. By the third quarter of 1938 such exports in some of the smaller component categories had already reached or exceeded targets.

The value of machinery exports at the end of the third quarter had already exceeded the monthly target value of 22.06 million pounds[7] for the end of 1948. Machinery export targets of 228 percent of 1938 volume for the end of 1949 require further increases in machinery exports as compared with 1948.

Exports of vehicles have also exceeded the increased monthly target value of 21.1 million pounds[7] for the end of 1948, and the volume of exports during the third quarter of 1948 had already approximated next year's target.

Exports of engineering products to the Western Hemisphere had particular success during the first three quarters of 1948, having increased the volume going to the Western Hemisphere over both 1938 and 1947:

Period:	Percent
1938	8.7
1947	9.2
First quarter 1948	11.1
Second quarter 1948	10.4
9 months 1948	12.7

Despite the interest in expanding exports of these goods, the United Kingdom had also budgeted carefully to meet domestic requirements with the minimum expenditure of foreign exchange.

Imports of engineering commodities will be at their peak in 1948–49

[7] £1=$4.03.

and can be expected to decrease thereafter. The general import policy is to restrict such imports if they can be obtained in the United Kingdom within a reasonable period of time. A freer import policy would probably mean increased availability of capital equipment at an earlier date. As indicated above, the export level for 1949–50 is roughly equivalent to the rates to be achieved by the end of 1948, increases in production thereafter should be available for domestic use if reduced world demand for semidurable goods by 1950 does not require increased shipments of capital goods to maintain the same level of exports for the industry as a whole.

g. Shipbuilding.—Production in British shipyards during 1948, estimated at 1.2 million tons, was substantially above the prewar level and higher than at any time during World War II with the exception of 1942. However, it was still well below the optimum efficiency level estimated at 1.7 million tons.

At the close of 1948, tonnage under construction and on order, totaling 4.5 million gross tons, was equivalent, at the present rate of building, to approximately 4 years of work. Approximately one-third of the work is for foreign account. The export of these vessels will bring in an average of approximately 110 million dollars annually over the next 4 years. Deliveries on domestic orders will add to the earning power of the merchant marine and help narrow the deficit in the balance of payments.

The industry faces a number of current problems including shortages of materials, faulty flow of component parts, higher costs of supplies, multiplicity of designs, and others. These, in turn, have contributed to higher costs of ships, slower delivery, and reduced productivity. Increased efficiency should be expected during the recovery period as the supply of materials and parts improves and competition for orders becomes keener.

h. Chemical industry.—The British chemical industry is the second largest in the world. The total value of manufactures of chemical and allied products in 1946 was 1.2 billion dollars and output since then has increased steadily. Production during the first 9 months of 1948 averaged about one-fifth higher than 1946.

The volume of chemical exports has risen sharply and since the first quarter of 1948, the total volume has been more than 50 percent above 1938. The significance of the chemical industry to the British export drive, however, cannot be measured by volume or value of direct exports. Chemicals also contribute indirectly as raw materials in scores of exported products.

The expansion of the British chemical industry is important not only in exports, but will also help to reduce dollar requirements.

i. Agriculture.—Out of the 31.7 million acres of crops and grass in the United Kingdom in June 1939, 18.8 million acres were in permanent grassland and 4.1 million in temporary grassland, leaving 8.8 million acres, or about 28 percent, in tillage. Agricultural activities employed approximately 5 percent of the manpower in civil employment. As a result of the wartime necessity to increase home production, tillage increased and permanent grasslands were reduced approximately one-third.

Balance of payments difficulties and the increased population to be fed have prevented the United Kingdom from reverting to reduced levels of agricultural production; on the contrary, increased activity is projected and investment in agriculture will take 5 to 6 percent of the investment program for 1948–49.

The 1948–49 program for agriculture calls for an increase in production of 30 percent over prewar, as compared with output during the preceding crop year about 20 percent higher than prewar. Mechanization of British farming since 1938 has made it possible to produce good yields per acre on soils previously considered too heavy for efficient cultivation.

Production figures for the harvest of 1948 indicate exceptional levels and major crops already harvested have on the whole achieved or bettered targets:

Crop:	*Production compared to prewar=100*
Bread grains	136
Coarse grains	193
Potatoes	225
Sugar (beet root)	120

By the fourth quarter of 1948 it appeared that targets for cattle, poultry and sheep production would be achieved and only hog production fall below target. Nevertheless, total livestock production is far below the prewar average. Although cattle numbers have increased over prewar, sheep and pig population is still below prewar levels because of set-backs in the program due to the severe winter of 1947, and the tight world supply situation in coarse grains.

Agricultural production has benefited from the employment of foreign farm workers. At mid-1948, it was estimated that there were approximately 32,000 ordinary foreign farm workers and about 20,000 former prisoners of war who had stayed on as civilians in agricultural employment.

j. Internal transportation.—The British internal transportation system suffered from the strain of the war, but today rail freight traffic, as measured by net ton-miles, is well above the prewar level and is likely to remain high. Passenger traffic has fallen steadily since 1945 and is now substantially less than in 1937, the peak prewar year.

Wartime arrears in maintenance of permanent ways have hindered railroad operations during the last 3 years; inroads on this backlog will probably be limited for some time because of steel and timber shortages.

The rolling stock position has improved steadily during 1948, but more than a quarter of the freight cars are over 35 years old. Although a replacement program is under way, it is also limited by the steel shortage and by export quotas set for private railroad equipment contractors.

Other forms of transportation are also carrying increased loads. The tonnage shipped via inland waterways has increased 11 percent over 1947, and motor transportation is expanding. More trucks probably would be in use if more than 55 percent of the commercial vehicles produced were not being exported.

The railroads, inland waterways, and road transport were nationalized on January 1, 1948, and today plans for modernization and integration of operations are still largely in the formative stage. There has been some evidence of improved handling of rail traffic and more efficient use of freight cars. Rail costs, however, are becoming a problem, and despite increased rates, the railroads incurred a loss during 1948 since traffic receipts were less than anticipated.

k. Merchant marine.—Wartime losses of British merchant ships (aproximately 11 million tons out of a gross merchant tonnage of 17.4 million tons at the outbreak of the war) have been largely replaced by new tonnage. At the end of November 1948, however, the total merchant fleet under United Kingdom and Colonial registry was still approximately one million tons short of prewar.

Shipping has been an important contribution to earnings on invisible account. Dry cargo earnings are above prewar since shipping rates have risen, but the parallel rises in commodity prices have reduced the purchasing power of this income. Net foreign earnings on dry cargo shipping more than doubled in 1948 compared to 1947.

2. Imports

For the United Kingdom, traditionally an importing nation, an adequate supply of imported food and raw materials is essential to maintenance of production. The value of merchandise imports was equivalent to 16 percent of the gross national product both in 1938 and 1947. Nevertheless, today by virtue of the United Kingdom's reduced financial position, the direction of effort is toward the maintenance of generally higher levels of activity with reduced dependence on external resources.

Thus, retained imports during 1948 were held down to less than 85 percent of 1938 volume. This is nevertheless a substantial increase over 1946 and 1947, when supplies moved in only very slowly and industrial activity unquestionably reflects this. The change is illustrated in the table below:

Index: Volume of retained imports

	1938=100
1946	68.3
1947	77.4
1948:	
First quarter	80.4
Second quarter	81.0
Third quarter	81.9

Total imports proposed for 1948–49 were intended to allow an increase in volume of 9 or 10 percent over 1947, approaching a maximum of 85 percent of 1938 volume.

Beyond this increase in the flow of goods a very significant shift in the sources of imports was proposed in the program. Under the abnormal conditions of 1947, the value of imports on dollar account amounted to 36 percent of the import program; the 1948–49 program as revised in the OEEC at Paris called for imports on dollar account of approximately only 20 percent of total imports.

While the dollar problem has been the most obvious one, the United Kingdom has also had a problem of balances with those Western Hemisphere countries where it has still been able to trade in sterling and which in 1947 supplied it with an additional 10 percent of total imports, consisting primarily of foods and some important raw materials. The 1948–49 program proposed to restrict purchases from these areas as well, in order to approach as nearly as possible self-supporting levels of trade.

The total impact of the United Kingdom import program for 1948–49 on the Western Hemisphere would therefore be of a magnitude somewhat in excess of 2 billion dollars, amounting to approximately 28 percent of the total import program. Imports from the Western Hemisphere at an annual rate of 2.4 billion dollars during the first half of 1948, amounted to 33 percent of the total import program, indicating what progress had already been made in this direction.

The United Kingdom expects to compensate for the shift of demand away from the Western Hemisphere in several ways: (*a*) By increased home production, (*b*) by an attempt to return closer to the prewar channels of trade, and (*c*) by development of resources overseas. To this end increased purchases from non-Western Hemisphere areas must be realized to compensate for the proportionate reduction in Western Hemisphere shipments. To meet the problem of exchange with other nonparticipants outside the sterling area, where a deficit can also be expected, raw materials from the rest of the sterling area are relied upon.

Composition of the import programs must change also if a high level of activity is to be sustained with reduced import totals. Since imports of raw materials must be protected to the maximum extent possible to allow for the increased level of industry, it was recognized that food imports, which constituted 50 percent of the Western Hemisphere import program in 1947, would have to be reduced in proportionate terms.

The shift from undue reliance on dollar food imports is illustrated in the table below, as is the reduction in emphasis on food. The total food import program for 1948–49 was expected to reduce this proportion still further.

Percentage of imports devoted to food, feed, and tobacco [1]

	Western Hemisphere imports	Total imports
1946	65.5	57.1
1947	52.7	49.9
1948: First half	51.3	49.6

[1] Cmd. 7520.

Substitution of sources for essential raw materials is more difficult than substitution of sources for food. To illustrate, Britain must continue to rely on dollar fibers and ferrous and nonferrous products to provide an adequate total supply. For some of these, indeed, the import program is less a matter of dollars or requirements than of inadequate physical availabilities. The effect of availabilities of goods had already been taken into account by the British in setting up their program. Supply developments since that time, however, suggest some adjustments may have to be made.

The anticipated adjustment of world food prices, as supply and demand approach a balance, can be expected to benefit the United Kingdom in the long run as it will remain a heavy importer. However, price adjustments in this immediate period can be expected to have only a limited effect, since United Kingdom procurement of bulk staples is largely on a contract basis with prices already determined. Raw materials procurement is affected by varying trends for the balance of the 1948–49 program but little price relief can be expected in the balance-of-payments sense, without fairly marked general decreases.

C. EXTERNAL BALANCE OF PAYMENTS

1. The Balance of Payments Crisis

The serious extent to which the United Kingdom's financial position had deteriorated by the end of World War II has been outlined earlier. Factors suggested were loss in exports, loss of the net income formerly received from invisibles; damage to industrial plants, abnormal dependence on imports from hard-currency areas, deterioration in the terms of trade, and others.

In the postwar years before 1948 the United Kingdom was faced with a deficit on invisible account for the first time.

Ever since the second quarter of the nineteenth century Britain had a deficit on merchandise trade more than balanced by earnings on invisible account. Income from foreign investments, shipping, insurance, banking, and tourism was greater than overseas expenditures on similar items, sufficient to allow the accumulation of very substantial foreign investments. After the first world war, this favorable position declined, and in 1938 the United Kingdom had a deficit on current account of 280 million dollars despite earnings on invisible account still in excess of 1 billion dollars.

During World War II this net favorable balance on invisible account was lost. Net receipts from invisibles in the decade before the war averaged about 925 million dollars a year, whereas in 1946 there were net payments on invisibles of 675 million dollars and in 1947 net payments of 775 million dollars. Not only were receipts reduced, but obligations to be met abroad were, as a result of the war, substantially heavier.

Two major factors aggravating the British balance of payments problem have been world inflation in prices and the deterioration in the terms of trade. Compared with the immediate prewar period, the terms of trade have shifted sharply to Britain's disadvantage. A volume of exports that paid for 100 units of imports in 1938, paid for only 92.6 import units in 1946 and 85.5 in 1947. Although there was a 1 percent fall in the level of import prices in September 1948 and an increase of 2 percent in the level of export prices, this movement was again reversed in October. This was principally because food imports were at last reflecting contract prices closer to world price on commodities such as Canadian wheat, which the United Kingdom had previously obtained at contract prices far below world price. The index of import prices (1938=100), stood at 296 in November 1948 and export prices at 258.

While the effects of progressive deterioration of the terms of trade should not be underrated, direct comparison with 1938 should be qualified. Analysis of export and import prices for the past century shows that Britain enjoyed more advantageous terms of trade during the 1930's than in earlier years, and a given volume of exports paid for roughly the same amount of imports in 1947 as it did in the 1920's.

a. Current account.—In 1946, with 5 billion dollars available from United States and Canadian credits, the United Kingdom expected to be able to finance deficits during the postwar period and achieve equilibrium in her international accounts by 1950 or 1951. The British had expected to incur a very heavy deficit in 1946 but had hoped to make steady reductions in the deficit in subsequent years. As noted earlier their 1946 position was much better than expected inasmuch as world conditions had prevented the anticipated flow of imports while exports had increased rapidly. The over-all deficit was only 1.5 billion dollars. However, in 1947 the situation deteriorated sharply as a result of factors beyond British control: Among these were rising price levels throughout the world, an exceptionally severe winter, precipitating an industrial crisis in the United Kingdom, and poor crops throughout much of the Eastern Hemisphere.

The British Government took strong measures to reduce the mounting deficit, but these did not take their full effect until near the close of the year. The British deficit on current account for 1947 exceeded 2.5 billion dollars. In the first half of 1948, with the austerity program in full force and ECA assistance only beginning to emerge, the British reduced their over-all deficit to an annual rate of about 1.1 billion dollars. Although final data for the second half of the year are not yet available, further improvements are indicated.

b. Reserve position.—As a condition of the 1946 credit from the United States, the United Kingdom undertook to assume the obligation of converting currently acquired sterling for current transactions by July 15, 1947. Despite the growing drain on resources, this obligation was implemented. During the following weeks Britain lost more than 1 billion dollars and the rate of drain reached a peak of some 35 million dollars per day. In these circumstances there was no alternative to a suspension of the convertibility privileges and following conversations with the United States unlimited transfers to dollar accounts were halted. After suspension there was still the task of reducing the drain upon gold and dollar reserves which had resulted from the United Kingdom current account deficit with the dollar area, and from the deficit of sterling area countries. The United Kingdom did not feel it was possible to suspend convertibility for sterling area countries, but arrangements were made with the rest of the sterling area to restrain dollar requirements. As these measures became effective, the drain on central reserves diminished in the first half of 1948 to 1 billion dollars, or an annual rate of about 2 billion dollars, which compares very favorably with a drain on gold and dollar resources of 4.1 billion dollars in 1947. The major part of the 1948 drain will be covered by ECA financing.

As a result of the gold and dollar settlements necessitated in the circumstances described, central reserves of gold and dollars had declined to a little over 2 billion dollars by the beginning of 1948, about half the figure for 1938. British concern over such losses is a major determinant in trade policy. The desire to keep expenditures within the limits of current hard currency earnings and ECA aid is reflected in United Kingdom programs drawn up under ERP. During the early part of 1948 the outstanding balance of the United States loan under the Anglo-American Financial Agreement was exhausted, and the United Kingdom also drew on the Canadian credit, the International Monetary Fund and a gold loan from South Africa. ECA reimbursements received during 1948 were almost equal to these sums. As a result of these aids, central reserves of gold and dollars were reported as 1,850 million dollars at the end of 1948, approximately 200 million dollars lower than at the beginning of the year.

2. The Deficit on United Kingdom Current Account for 1948–49

Final data for 1948 are not yet available, but at the levels of trade which prevailed during the second half of the year, the United Kingdom deficit on current overseas account can be estimated at less than three quarters of a billion dollars. An estimate for 1948–49 suggests approximately similar levels for that period also. The deficit on current dollar account is estimated at 1.1 billion dollars. These figures represent a very considerable reduction over 1947 when the total current deficit on United Kingdom account was 2.5 billion dollars including a deficit with its own dependent overseas territories of more than 200 million dollars; the deficit on Western Hemisphere dollar account was 2.4 billion dollars.

In the frame of the British submission, the United Kingdom expected to have reduced demands upon nondollar Western Hemisphere sources to such an extent that the problems of financing in these areas would not create any difficulties. Estimates from available data suggest a maximum deficit about one-third that incurred in 1947. Sale of British owned railroads and associated transport utilities to Argentina during 1948 provided the major financing aid in this area. Negotiations for the sale of some of the United Kingdom's remaining utilities investments in Latin America have been under way for some time and if consummated may provide small amounts of additional funds.

If British expectation of supplies from other nonparticipating countries proves overoptimistic, it may be necessary to increase the proportion of requirements to be met in the Western Hemisphere. This would have obvious repercussions on the balance of payments position.

A feature of the United Kingdom balance has been the deficit with other nonsterling nonparticipants outside the Western Hemisphere, which rose from about 50 million dollars in 1947 to an annual rate of almost 450 million dollars during the first half of 1948. As indicated in discussing the shift of import demands away from the Western Hemisphere, this deficit can only be sustained on the assumption that other nonparticipants' sterling accumulations will be used for procurement of raw materials in the rest of the sterling area outside the United

Kingdom proper, or in the procurement of commodities from participating countries short of sterling.

The areas in which the United Kingdom expects to experience a surplus in 1948–49 will be the nonparticipating countries of the sterling area and the nonsterling participating countries as a group. Part of the surplus arises out of British contributions to postwar relief and rehabilitation. As for the rest, this group of balances will not be settled in gold or dollars, but will be met in part from accumulated sterling balances or from sterling acquired through movement of new capital to some of these countries. In 1947 the United Kingdom had a surplus with the nonparticipating members of the sterling area of 562 million dollars and its export of new capital was in excess of this amount. However, there was a deficit with the other participants.

For 1948–49 it has been estimated that the United Kingdom will have a surplus with the nonsterling participating countries in excess of 100 million dollars. These other participants will also incur a deficit with the nonparticipating members of the sterling area. The total sterling surplus was estimated at 521 million dollars. The United Kingdom is making sterling available to the other participants through the intra-European payments scheme to meet this gap. Grants of drawing rights originally totaled 312 million dollars and 209 million dollars were to be available by access to accumulated sterling balances. Since that time, the United Kingdom has also agreed, subject to OEEC confirmation, to extend 8 million dollars in drawing rights to Turkey. Belgium is making 30 million dollars in drawing rights available to the United Kingdom, so that the net drawing rights extended by the United Kingdom will amount to 290 million dollars. Australia has announced a sterling grant of 32 million dollars to the United Kingdom to aid in reducing the burden of these grants of drawing rights. For part of the balance, however, the United Kingdom will incur additional sterling obligations to the sterling area countries as a result of their surpluses with participants.

The impact of the intra-European payments scheme on the United Kingdom proper as a supplier is thus expected to be less than on a showing of gross magnitudes. In terms of the economy as a whole, it will gain by the additional tonnage of Belgian steel (100,000 was the first estimate and it may be as much as 300,000 tons) that will be available to it at least in part for drawing rights.

One consequence of the projected sterling area surplus with the other participants is the probability that sterling will become an increasingly hard currency to most of these countries. They should therefore be willing to accept sterling in trade with any area and an impetus would thus be given to the restoration of sterling in international trade.

The question could be raised, however, whether the United Kingdom might not increase its imports of less essential commodities from countries expecting to be short of sterling, or relax its restrictions on travel. Increased supplies of such goods might aid in combating inflationary pressures, or might conceivably provide incentives to increased production. Psychological effects can hardly be calculated so nicely in statistical terms, but the result of any general relaxation of present austerities would mean an increase in the balance of payments deficit without consequent increase in availabilities of raw materials to meet the expanded requirements upon which further projected increases in the levels of production must be predicated. Similarly relaxation of travel restrictions is limited because of the necessity to reduce the hard currency drain to some of the other participants.

In making the calculations for 1948–49, prices assumed were those expected to apply during the period. For the United Kingdom, as stated, there had been a progressive deterioration in the terms of trade. Although export prices have also been rising, even if less rapidly than imports, serious price resistance has not been encountered so far, except for a small number of products in a few market areas. An adverse shift in the ratio of export prices to import prices may have similar general effects upon a country's competitive position as devaluation of currency.

For a substantial effect upon the balance of payments, there would have to be a much greater shift in the terms of trade in favor of the United Kingdom than has yet shown any signs of developing. Sharp immediate reductions in import prices might have a somewhat delayed effect upon the United Kingdom because its procurement of staples is so extensively on a contract basis with prices already determined or with the limits of price variation established for considerable periods in advance. Furthermore, a general and substantial decrease in prices of imported raw materials and food might require some reduction in the price of manufactured goods, thus reducing export proceeds and the available means of payment. Actually, however, there is little immediate prospect of such extensive readjustments and the possibility that increases in one price sector may compensate or more than compensate for decreases in another remains.

3. Capital Accounts

In addition to the current account deficit, the United Kingdom must meet certain capital charges in dollars, such as amortization payments on the United States RFC loan made in 1941, and other accounts.

From the United Kingdom estimate, it appears that the dollar earnings of the United Kingdom dependencies will show a very substantial improvement over 1947 and 1948. The dependent territories are, of course, included in the definition of participants for ERP purposes, although no specific programs are submitted for them because of the difficulties involved in building up detailed accounts and since, on balance, they earn dollars.

In calculating the United Kingdom position it was necessary, however, to consider not only United Kingdom accounts but also Britain's position as the financial center of the sterling area. Since the participating countries were interested in accommodating their total sterling deficits through the mechanism of the intra-European payments plan, and not merely that part of the deficit arising through transactions with the participating members, a unified treatment of the sterling area trade was suggested. As indicated above, the United Kingdom agreed to provide for the financing of the total participant deficit with the sterling area by granting drawing rights and by allowing access to past accumulations of sterling. In return for this aid to the other participants, the United Kingdom was allowed to consider the dollar position on total sterling area account in calculating aid requirements.

In 1947 the sterling area outside the United Kingdom incurred a dollar deficit of more than 800 million dollars net of current gold production purchased by the United Kingdom for sterling. This estimate then included countries which are no longer members, Ireland and Iceland which are ERP participants, and an allowance for South Africa which has agreed with the United Kingdom not to make net drawings upon the central reserves.

During the first six months of 1948, the deficit incurred by the sterling area outside the United Kingdom with the dollar area ran at an annual rate of 225 million dollars. Purchases of new gold from these areas, which should be deducted from the deficit, amounted to 36 million dollars. Gold production (excluding South Africa) for the year is estimated at 65 million dollars.

For the 1948–49 program, the United Kingdom estimates that the deficit of the nonparticipating sterling area with the dollar area will be canceled, in effect, by the net earnings of the dependent territories. It is clear that very substantial reductions in the impact of sterling area dollar needs upon the United Kingdom have been effected by a combination of ECA aid to the participating members, United Kingdom, Ireland, Iceland, and reduction of dollar requirements by the nonparticipants.

This, however, is not the sum of the demands upon the United Kingdom for hard-currency exchange since it may also have to make settlements on bilateral payments agreements to other participants and to nonparticipants, some of which were former members of the sterling area. Although it was recognized that payments of this type will have to be made, some elements of the accounts with nonparticipants have been excluded from consideration for aid as more suitably financed out of other United Kingdom resources.

Despite the action of the intra-European payments scheme, the United Kingdom expected to have to make hard-currency settlements under the terms of existing payments agreements with some of the participants. The United Kingdom has, as indicated above, a drawing right of 30 million dollars on Belgium. Judging from the rate of compensations to date, this could have been largely exhausted at the first monthly compensation under the scheme, but the United Kingdom elected not to include a gold payment already made in order to preserve some of the drawing right for a subsequent period. It was expected that settlements would have to be made with Belgium, Switzerland, and with The Netherlands. (The Netherlands payment is intended for the dollar deficit of the Netherlands West Indies.) The rate of settlements with other participants actually required during the first few months of the program year is far in excess of the allowance originally included, suggesting that net settlements may be more than twice as high. In reassessing requirements, only about half the minimum estimate of the excess was assumed to apply, to allow for the possibility of some intra-European adjustment and swings in the movement of trade and balances.

The United Kingdom also must provide for use of gold in industry, medicine, and the arts in the United Kingdom.

4. Status of reserves

United Kingdom official holdings of gold and dollars were about 2,050 million dollars at the beginning of 1948, excluding consideration of certain outstanding credits still available. The gold and dollar drain during the first 6 months of the year amounted to 1,025 million dollars, of which the United Kingdom deficit with the dollar area was 750 million dollars. This drain was met by drawings using up the balance of the United States credit of 1945, drawings on the Canadian credit of 1946, a gold loan from South Africa, drawings on IMF, and ECA reimbursements, so that the actual decrease in gold and dollar holdings during the 6 months was 150 million dollars. During the balance of 1948 central holdings of reserves declined an additional 60 million dollars despite ECA reimbursements of approximately 600 million dollars. While there are additional ECA allocations to the United Kingdom outstanding, they must in part cover transactions which are not yet reflected in exchange records and cannot be directly applied against the decline in reserves already incurred.

The estimate of the reserve position for 1948–49 depends, in addition, on the extent that gold payments must be made as net settlements under payments agreements not canceled by the intra-European payments scheme and not already allowed for. On the basis of present estimates, it seems reasonable to expect that the considerations enumerated may result in a further moderate reduction in British reserves of gold and dollars.

5. Allocation of Aid Funds for 1948–49

Present estimates suggest a total dollar account deficit for 1948–49 of slightly less than 1.3 billion dollars, after allowing for the use of Canadian credit and limiting the estimate for settlements with other participants as described.

The United Kingdom submission to OEEC requested an allotment on its initial budget program totaling 1,271 million dollars. This already assumed that credits would be available from Canada in the amount of approximately 60 million dollars. At this point a complete estimate of the general balance of payments was waiting on the discussions with the other participants and the results of the negotiations on the intra-European trade balances. The OEEC recommended aid to the United Kingdom of 1,263 million dollars. This figure allowed for the application of colonial dollar earnings to the nonparticipating sterling area deficit with the dollar area, and for the full dollar and hard-currency drain on other accounts as then estimated. The estimated ECA allotment of 1,239 million dollars is less than sufficient to allow for all of the hard-currency obligations of the United Kingdom as currently estimated for the period.

Actual allotments made to the United Kingdom to date have been:

Period or date:	(In millions of dollars)
April–June 1948	400.0
1948–49: for July 1948 to March 1949	919.1

Of this aid, 313 million dollars is being extended in the form of loans, 232.3 million dollars as conditional aid dependent upon extension of aid by the United Kingdom to the other participants under the intra-European payments plan, and the balance on a direct-grant basis.

As a result of the intra-European payments negotiations, detailed earlier, the United Kingdom will be making net drawing rights of 290 million dollars available to the other participants, to enable them to meet deficits with the sterling area. Although the necessity for some adjustments and revisions has appeared, the magnitude of the suggested sterling surplus appears to be substantially feasible, and the credits to be extended by the United Kingdom under the intra-European payments scheme will make for an effective sterling area contribution to the other European participants.

The gross aid of 1.239 million dollars for 1948–49 overstates the amount of direct net dollar aid to the United Kingdom since net sterling drawing rights are being extended by the United Kingdom to the other participants for 290 million dollars. However, ECA believes that the suggested allocation and the implied level of dollar aid for the United Kingdom is sufficient to support the proposed limited program in cosideration of the qualifications interposed in the discussion of particular sectors of the program. The impact upon United

Kingdom reserves of the remaining hard-currency drain is more than originally expected but the possibilities of further adjustment among the participants have not been entirely exhausted. ECA will continue its current review of the status of all programs, and will make such adjustments as are determined to be necessary.

One note of caution remains to be added: If the United Kingdom must return to Western Hemisphere markets to make up possible deficits of supply from other nonparticipants, this evaluation of its position may have to be reconsidered.

D. INTERNAL BALANCE OF FINANCE

1. Introduction

The Economic Cooperation Act calls upon each participant to adopt policies which will create and maintain internal financial stability. In the United Kingdom government policy also is directed to this end.

The government budget was brought into balance in the fiscal year that ended just at the time the ECA Act was signed. This year, there will be a substantial surplus. Price levels and the cost of living are rising only at moderate rates. The total money supply rose only between 1 and 2 percent in the year following the sterling crisis of August 1947 and credit expanded about 5 percent. Wages, distributed profits and dividends have been subject to limitation of increase by voluntary agreements.

As a result of these and other measures, and despite the expanded inflationary potential created during the war and postwar period, public confidence in the internal value of the currency has been maintained, and the financial foundation for a successful recovery effort has been laid. This does not mean that all inflationary pressure has been eliminated. The planned budget surplus may not be realized in full; the investment program for 1948 is considerably larger than the reduced program called for; the volume of private savings seems to be declining rather than growing as would be required to balance the national account without inflation. Pressures are, nevertheless, comparatively mild and have not prevented the attainment of production, export, and investment goals.

2. Experience in 1948

The experience of the United Kingdom in 1948 demonstrates that while the principles on which the government is operating may be correct, the desired results have not always been fully achieved. Deviations from estimated trends have not, however, reached unmanageable magnitudes.

The following table, based on the government's economic survey for 1948 and budget estimates, suggests that on early estimates of activity voluntary private savings would have had to amount to 1.4 billion dollars to prevent inflationary pressures from increasing.

Capital account of the United Kingdom for the fiscal year April 1948–March 1949

	March 1948 estimate (economic survey) (in billion dollars)
1. Gross domestic capital formation	7.2
2. Less depreciation allowances [1]	3.2
3. Net domestic capital formation	4.0
4. Savings from government sources [2]	1.6
5. Net overseas resources	1.0
6. Total, 4 and 5	2.6
7. Private savings needed to balance capital account	1.4

[1] This allowance understates possibly as much as 20 percent since there is general agreement that the cost of making up wear and tear has risen probably by 25 percent. See Paish, Westminster Bank Review, November 1948; Financial Times, November 9, 1948.

[2] This item includes central and local government savings and is not comparable with budget surplus.

As the fiscal year progressed, however, several developments, all tending to increase inflationary pressures, had become sufficiently apparent to distort the specific estimates on which the budget was originally based. It was officially admitted by September that the capital expenditure program for the budget year was running at a rate of at least 8 billion dollars or 800 million dollars above the economic survey estimate. The net movement of the savings side of the account seemed to be downward, rather than upward, as would be required to balance the account without inflation. It seems likely that the overseas deficit for 1948 will fall considerably below the 1 billion dollars originally shown in the economic survey. Savings from government sources (central and local government savings), originally estimated at 1.6 billion dollars and intended to fill the savings gap as then estimated, will probably not reach this level. Food subsidies are running more than 300 million dollars higher than the budget estimate, health services are costing more than had been anticipated, and the new defense program has been estimated as costing roughly 200 million dollars additional annually, excluding pay adjustments to the forces. Revenues, however, have run somewhat ahead of expectations.

The increase in capital formation and decrease in government savings relative to the estimates, will probably not be matched by a compensating increase in private savings. Under the revised estimates these would have to rise very substantially in order to offset the capital investment program without inflation. The partial data available, even after allowance for increased private savings in the second half of the fiscal year, suggest an increase of the indicated magnitude is unlikely.

In spite of the adverse developments discussed above, the internal financial position of the United Kingdom has been characterized as remarkably stable in view of the general situation facing the economy. The past year has seen the country meeting ambitious targets for exports, surpassing original programs for investment, and providing an increasing volume of commodities for other uses, while prices have risen only modestly.

E. FINANCIAL SITUATION AND POLICIES

1. Fiscal Policy

Fiscal policy is recognized in the United Kingdom as a major instrument for assuring the financial stability essential to recovery. Although, as stated above, the budget was in balance in 1947, underlying inflationary pressures threatened the wage-cost-price structure and the government adopted a policy of reducing such pressures by budgeting for a substantial surplus through maintaining tax revenues and reducing expenditure. The budget as announced in April 1948, for the fiscal year ending March 1949, proposed a true surplus of 1.3 billion dollars, with total ordinary revenues estimated at 15.2 billion dollars, total ordinary expenditure of 11.9 billion dollars and allowing for capital expenditure by the government. Although this would have been sufficient to offset the inflationary impact of the export drive for the year, rising expenditures, largely attributable to increasing import prices which have necessitated increasing expenditure on subsidies, and an increase in the defense program and civil estimates may prevent realization of the full amount. However, a substantial surplus should still be realized.

2. Government Revenues

Government revenues are being sustained by high taxes. Direct taxes such as the personal income tax and corporate profits tax are expected to produce about 8 billion dollars. In addition more than 6.4 billion dollars will be collected in indirect taxes such as customs, purchase taxes, automobile taxes, and others. Purchase taxes on luxury goods are very high with rates ranging from 33 to 100 percent. Direct and indirect taxes and local rates together amount to $315 per capita, which compares with $380 per capita in the United States covering similar taxes. Inasmuch as per capita national income in the United Kingdom is only roughly half as high as in the United States, taxes are a heavier real burden.

This tax policy is adopted in deliberate recognition of its disinflationary effect.

The Exchequer position at the end of November, after 8 months of the budget year, was some 800 million dollars better than at the corresponding time in the preceding year when the budget balanced. Increasing receipts during the latter part of the fiscal year may improve the revenue position still further.

3. Government Expenditure

While the government has budgeted for a surplus to reduce inflationary pressure, there are still heavy expenditures to be met. Among the major categories of government expenditure financed by tax revenues and shown below, there seems to be little hope for substantial reductions in the immediate future.

Major expenses to be financed by tax revenue April 1948 to March 1949, Budget presentation

	(Value in billions of dollars)		(Value in billions of dollars)
Debt service	2.0	Education	0.8
Defense	2.8	Food subsidies	1.6
Health and housing	2.16		

Service on the public debt is at an average interest rate of 2 percent, and although there is a policy of retiring short-term debt, the interest saving will be small since this category of debt usually earns less than 1 percent a year. (Local currency counterpart funds are being devoted to the retirement of short-term debt.)

While the health, housing, and education programs have some inflationary effect, it is clear that a good part of such expenditures by the Government represents a transfer to Government account of payments which would otherwise be financed out of individual budgets, rather than a wholesale increase in these activities. The social services program also provides obvious benefits to the economy by maintaining health and morale to the benefit of increased productive effort. Much of housing construction is being directed to areas where increased activity makes it necessary to attract and keep an increased labor force. On the whole, the physical requirements of such programs are virtually at a minimum.

The subsidy program, assisted by other controls, had been successful in restraining the rise in the cost of living during the war period, an important factor in preventing runaway increases in production costs. The Government, in setting its economic programs for 1948, established an anti-inflationary policy calling for voluntary agreements to prevent general increases in wages, salaries, and personal income from profits, rents, or other sources. Trade-union support for this policy was predicated on the understanding that living costs would not be permitted to rise excessively.

In addition to food subsidies, smaller amounts are expended to prevent the full effect of price increases in imported raw materials from disturbing the internal price structure. Should import prices fall, the subsidy program could be tapered off gradually without disturbance to the internal cost structure. If prices continue to rise some additional part of the burden may have to be passed on to the consuming public. However, increasing production and attendant economic development under the recovery program may increase the general ability to bear the burden of taxation.

4. Debt Retirement

The Government has placed major emphasis on retiring the short-term debt as the most direct way to fight inflation since it is so closely associated with purchasing power held by the public. The United Kingdom has in the past used its net income from exchange operations to reduce the public debt. In the fiscal year ended March 31, 1948 (just prior to the enactment of the Economic Cooperation Act), 3.2 billion dollars of the sterling counterpart of United States, Canadian and South African loans, contracted to help finance overseas deficits, were used to retire internal debt. Although the budget balanced, short-term internal debt was reduced by 1.64 billion dollars and long-term internal debt by 1.56 billion dollars. During the present fiscal year the greatly decreased balance of payments deficit will limit the availability of funds from this source. Under the Economic Cooperation Act a special account is established for 95 percent of the local currency counterpart of ECA aid, and is intended to be used for purposes furthering recovery objectives. To date these funds have been devoted to further retirement of short-term debt. Such repayments, through December 31, 1948, amounted to 330 million dollars. Short-term debt retirement during the budget year will probably equal the record of the preceding year, partly because the Exchequer will have the added funds becoming available by realization of the budget surplus, and partly because no long-term issues mature.

5. Money and Prices

Although huge inflationary pressures were generated during the war, Britain's cost-price structure rose very slowly, reaching a level about 50 percent above prewar at the end of hostilities. This was a smaller relative increase than experienced by other belligerents and was accomplished by a combination of subsidy and price control technique formulated to avoid repetition of the cycle of price and industrial disturbances following the First World War.

Since the end of the war, costs and prices have continued to rise at a rate of about 10 percent a year, reflecting the continuance of inflationary pressure in the economy. Further gradual increases are to be expected, since it is hardly possible to avoid upward adjustments entirely in an inflationary situation. However, over-all financial stability should not be threatened by such price movements.

It is not possible to predict exactly the structure of future British budgets, movements of prices, or changes in money supply. Too much depends on the changing character of the international political scene, import-price movements, world-export markets, and other unpredictable factors. However, the United Kingdom is pursuing responsible fiscal policies which are consistent with the Economic Cooperation Act and which are designed to provide the financial framework for a sound recovery.

The policies of providing a budget surplus to counteract inflationary pressures and supplement private savings, restraining the upward movements of wages, salaries, and profits and using the proceeds of ECA aid to retire debt all help to create a remarkably stable internal situation, in spite of the purchasing power generated by the export drive and the capital-investment program. Whether these devices will be sufficient to maintain a stable cost structure in later years, when the overseas deficit will be even lower, is a problem to be faced by the British Government. The British may ultimately have to reduce net investment and/or reduce the volume of export trade in order to curb inflationary tendencies. These steps would slow the rate of apparent recovery, but some of them may prove necessary to stability. In the coming year, however, it is apparent that inflation will not be permitted to disrupt the continued recovery of the United Kingdom.

F. THE BALANCE OF RESOURCES

1. Gross National Product

Further growth in the United Kingdom's gross national product can hardly be as rapid as the recovery of the last 3 years, but there is general agreement that there will be steady improvement. While none of the United Kingdom programs specifically states the expected rate of progress, a rate of 2 to 3 percent a year is indicated as reasonable; in the OEEC discussions, the United Kingdom stated that planning was based upon a figure of 2½ percent per year. While 2½ percent per year would be a high rate for a long period, it is probably conservative for the time interval under consideration, particularly in view of the intensive effort toward modernization. There are indications, however, that gross national product may increase at a greater rate than estimated by the British.

In the following table two alternative assumptions have been made for 1948–49:

"A" assumptions.—National accounts estimated to conform as closely as possible to official statements and estimates. GNP rate of increase, 2.5 percent p. a. Government consumption stable.

"B" assumptions.—More realistic or more desirable alternatives; GNP rate of increase, 3 percent p. a. Government consumption to increase.

All assumptions derive personal consumption as a residual. Net contribution from overseas from British estimates of early fall 1948 tends to overstate actual by about 0.2 to 0.3 million dollars.

Distribution of available resources (1948 prices)

[In billions of dollars]

	1948 [1]	"A" assumptions, 1948–49	"B" assumptions, 1948–49
Resources available:			
GNP	$41.4	$41.9	$42.0
Compounded Index	100	101.25	101.5
Net contribution from overseas	$1.0	$1.0	$1.0
Resources available for home use	$42.4	$42.9	$43.1
Index	100	101.2	101.6
Allocation of use:			
Gross domestic investment	$8.7	$8.0	$9 0
Percent distribution	20.4	18.6	20.9
Index	100	92.0	103.4
Government consumption	$7.7	$7.7	$7.8
Percent distribution	18	17.9	18.1
Index	100	100	101.3
Personal consumption	$26.1	$27.2	$26.3
Percent distribution	61.5	63.5	61.0
Index	100	104.2	100.8

[1] 1948 estimate, based on Barna, Financial Times.

NOTE.—All numbers rounded.

Since official estimates for the current year are probably less than actual, the projected total for 1948–49 on "A" assumption, above, appears lower than current. The residual, personal consumption increases less on "B" assumption since investment increases as it should be expected to do. The "B" assumption would appear to be a more realistic estimate.

2. The ECA Contribution

A straightforward comparison suggests that ECA aid for 1948–49 is equivalent in value to the estimated annual increment in gross national product on "B" assumption. It helps to finance approximately 15 percent of the essential flow of food and raw materials that make this level of activity possible. Inability to obtain such supplies would mean cuts in all elements of the program; investment would lag and the levels of production could be expected to fall sharply because of the interruption in supply.

G. EFFICIENCY AND PRODUCTIVITY

1. Productivity of Labor and Capital

The United Kingdom can no longer hope for increased production stemming from increases in the labor force. While there is no present general shortage of labor, specific industries have not been able to attract the increments desired despite government efforts to increase essential employment at the expense of less essential activities. If planned increases in production are to be realized, increased industrial efficiency and improved productivity are mandatory. Increased production through increased working hours and better distribution of labor are in themselves unlikely to be adequate.

Wartime disruptions adversely affected productivity rates, but official announcements have suggested that output per man-year has recovered to prewar levels. Naturally the position varies from industry to industry, and while some, such as the metals trades, have increased labor productivity, others, principally cotton textiles, building materials, construction, transport, and coal have not yet regained the prewar levels. It is hoped that hindrances to a smooth flow of production stemming from shortages of materials and components will be reduced during 1948–49. While an improvement in industrial productivity may be predicted, there remain real questions of degree of achievement and relative levels of cost.

Under the impact of war and postwar conditions, the British labor movement interest in production is increasing. Agreement reached between the Government and trade unions during the war to suspend restrictive practices has carried over into the postwar period. The top-level labor leadership now advocates an all-out production effort. While there are still fears of unemployment in the ranks and some resistance to change, the situation is becoming one in which an aggressive, alert management, working through consultation with local unions and employees, can count on support and cooperation.

Since the end of the war the United Kingdom has been relatively free of industrial stoppages so that losses of production due to this factor have been insignificant. So long as the cost of living is kept fairly stable it is safe to predict that industrial unrest will be held to a minimum. Absenteeism has, however, been a problem, especially in coal mining.

The demand for the 5-day, 40-hour week, one of labor's fundamental demands for the postwar period, has been reduced, because of the country's economic difficulties, to 44 with overtime pay for excess hours. The desire for shorter hours persists, however, and some downward adjustments in the standard workweek are taking place, although, except for women and juveniles, the actual hours worked have not been reduced materially. The effect of the shorter-hours movement has been largely an increase in overtime work. Average hours actually worked in the United Kingdom are now about 46½ for men compared with about 47½ in 1938; for women and juveniles, hours worked are now 42 and 41, compared with about 44 and 43, respectively, in 1938. If materials and power were available, permitting more overtime working, there are many factories where the workers would be willing to work the extra hours. In textiles, however, longer hours have not been entirely successful because of the large number of women operatives who have family responsibilities to meet.

While wages have been consistently lower in the United Kingdom than in the United States, the industries in which the United Kingdom is most successful in competition are those in which productivity is relatively high rather than wages low, in comparison with other British industries.

With full employment, bonuses and overtime, combined with increased wage rates, average weekly earnings in industrial employment have better than doubled compared with 1938. The cost of living, indicated by linking slightly disparate series, has risen about two-thirds as much. Essentials remain subject to controls and the contribution of food subsidies to limiting the full effect of increases in world prices is important. Rationing effectively limits inequities in distribution of essentials. Price increases in nonessentials have, of course, been marked. However, there is good reason for believing that real income for lower income groups has improved.

Employer interest in increased efficiency is also rising. In many industries the introduction of new machinery, the rationalization of design and production methods and the expansion of plant facilities are being pressed. The limitations here are largely physical and arise from the difficulty of securing new machinery, more power, building materials to expand plants, and other necessities.

The whole concentration of effort, however, must not be upon the addition of more tools and the British are well aware of this. Programs for redeployment of the labor force to utilize existing equipment are under way. The problem particularly affects textile plants where there are plans for regrouping and rearrangements within plants which have demonstrated their effectiveness. Accession by the industry is on a voluntary basis and has been less rapid than could have been desired. The area of endeavor is one in which the work of the Anglo-American Council on Productivity, which consists of American and British representatives of management and labor, may be especially helpful.

With an increase in supply of raw materials, the expansion of plant facilities, construction of new plants and an increase in the supply of power, the physical limitations on production should tend to diminish. If full employment is maintained, both labor and management will be encouraged to press for higher productivity.

The unfavorable factors to be taken into account are problems of costs rather than increased production. In the present seller's market where practically anything that can be produced can still be sold either at home or abroad, price has not been a primary consideration. There has, therefore, been no great incentive to concentrate on reducing costs of production. In consequence costs generally have been rising, and in some cases it is already clear that Britain will have difficulty in maintaining exports in competition with other countries unless the cost problem can be solved: For example, coal and textiles, which prior to the war were confronted with this difficulty, are likely before long to encounter serious competition in the international markets.

The high level of taxes as it affects both labor and management would appear to exert a depressive effect on the incentives to increased earnings that might result from increased productivity. During the current budget year (ending March 1949) there were some readjustments of income tax rates, the effect of which was to exempt 500,000 lowpaid workers, and by increasing the proportion of tax-free exemption and lowering rates for employed married women, the net effect was to lower rates for all incomes, with greatest effect on lower and middle-bracket incomes.

The physical availability of consumption goods, however, remains quite limited, and as long as consumption in the United Kingdom must remain restricted to favor exports or investment, little relief can be expected in this sector. Tax relief without substantial increases in domestic supplies of goods seems more likely to add to price problems than to relieve them.

2. Distribution

In the United Kingdom, the distribution of goods and services is proceeding in orderly fashion. Because of the effective progress in recovery which the United Kingdom has made, and because inflation has been well controlled, distribution presents no serious problem. The public has generally accepted price controls and rationing. This is in distinct contrast with certain of the other European economies where scarcities, inflation and black markets have disrupted distribution, drawing an abnormal number of individuals and firms into trading activities or causing the agricultural population to withhold products from market. It is fully expected that orderly distribution through regular channels will continue in the United Kingdom throughout the period of ERP.

The efficiency of the distribution system has steadily improved. Agricultural and industrial production are both substantially above prewar levels, meaning an increased volume of goods to be distributed, and the number of individuals engaged in distribution has declined nearly 20 percent. The proportion of the total labor force engaged in distribution has also declined, from 15½ percent in 1939 to 12 percent in 1948.

At the same time, it should be noted that British efforts to withdraw additional workers from low priority occupations such as distribution have not achieved targets, even though these targets are modest. These are clearly small magnitudes, however, and the general situation with respect to distribution in the United Kingdom is a comparatively favorable one.

3. Incentives to Investment

Investment, modernization and increased productivity are so basic to recovery in the United Kingdom that the question of incentives to private capital formation is extremely important.

The United Kingdom depends largely on voluntary private investment. Many controls affecting capital formation are operative, but they are largely negative in character; i. e., the Government may not allow steel for certain uses, may refuse building permits, or restrict stock issues. The Government thus has wide powers for preventing private investment where it is deemed undesirable from an over-all recovery viewpoint. But where willingness to modernize is deficient, controls and Government measures have a far more limited effect. In the case of nationalized industries, of course, the Government takes positive action to realize capital improvements. This is also true of housing, which is carried out almost entirely by local authorities. In the development areas construction of plant and commercial buildings is also undertaken. For the rest, modernization in the United Kingdom depends on private investment. To some extent the Government does encourage private investment in particular fields with indirect incentives, such as the price-support programs in agriculture and the subsidy system used in textiles, where groups of mills agree to undertake improvements according to governmental plans.

At the present time, and for the foreseeable future, there appears to be no lack of willingness to invest in general. The problem in the United Kingdom is rather to curb total investment to levels which productive capacity can support, after allowing for necessary consumption and Government use of resources, both civilian and military. During the past year several measures have been taken to restrict the total volume of investment and to direct it into lines considered most essential. Housing, new building for the health, social services, and educational programs have been curtailed in favor of rebuilding and expanding industrial capacity. Even so, it is expected that total investment will be even greater than the United Kingdom has estimated.

While taxes, as any subtraction from profits, lessen incentive to invest, tax policy appears to be only a relatively minor element affecting decisions to invest during the ERP period. At the end of the war the United Kingdom, just as did the United States, repealed its excess-profits tax on corporations. It is estimated that at the end of 1948 profits after business taxes of all sorts were somewhat increased over 1947, and were substantially higher than in 1946.

The normal tax on profits remaining in the United Kingdom is

25 percent on distributed profits and 10 percent on undistributed profits. Therefore, depending upon the portion of profits paid out, the normal profits tax varies between 10 percent and 25 percent compared with the 40 percent normal rate in the United States. This tax structure has in general been designed by the United Kingdom to promote investment. Firms are encouraged to reinvest income, since on retained, reinvested earnings, the tax is only 10 percent; on dividends paid out it is 25 percent.

Personal income taxes in the United Kingdom are higher than in the United States. However, capital gains, unless made in connection with a regular business, are treated in the United Kingdom as casual income and not taxed at all. The United Kingdom has no local income taxes.

For the country as a whole, total Government expenditures take up a large proportion of the gross national product in the United Kingdom, which means, on the income side, that more of total income goes for taxes. However, government expenditures in the United Kingdom are an integral part of general fiscal policy, a major aim of which is to steady economic fluctuations. Success in this fiscal policy would lend impetus to investment in the future.

Both before and after taxes, the proportion of total United Kingdom income comprised by interest and profits has shown little change since before the war. Since this is a constant proportion of a rising real national income,[8] it indicates a gain in real income since the prewar period for recipients of profits and interest.

For the next several years, therefore, it may be expected that incentives to investment will in general not be deficient, but on the contrary will be high enough to stretch productive resources and to require continued restriction and direction into the most essential lines. The effects of labor rigidities and taxes are in some cases restrictive, but are not controlling in the over-all picture. More important are views of the future of the United Kingdom and its ability to compete in world markets and the course of world trade and prosperity.

In spite of this general pressure for investment, however, investment in plant and equipment in particular industries is below desirable levels, for example, in textiles where private capital appears loath to undertake the risks involved in comprehensive reorganization and modernization. The outlook for United Kingdom exports in world markets in this industry as well as others is one of the governing factors in capital formation.

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[8] Bulletin of the Oxford University of Statistics, October 1948, p. 309.

II. POLITICO-MILITARY SITUATION AS IT AFFECTS BRITISH RECOVERY

1. Political Considerations Affecting Recovery

The British Labor Government derives support from the organized trade union movement and from elements in agriculture, the professions and small business. The trade unions, recognizing that greater production is the key to economic recovery and full employment, are taking steps to encourage maximum labor participation in the drive for higher output. While the Government and organized labor approach industrial questions from somewhat different viewpoints, harmony prevails on the essentials of recovery policy. The trade unions have voluntarily undertaken to support the government's wage-price stabilization program by exercising restraint in pressing for wage increases, the 40-hour week and other long-standing aspirations for a higher standard of living, on the understanding that other personal incomes, derived from profits, rents, or other sources, will also be limited and low prices for essential items maintained by means of subsidies where necessary. Rationing of scarce commodities is an integral part of the program to control prices; maintenance of minimum levels of consumption at home, importation of foreign labor under certain safeguards, and other measures designed to expand exports and bridge the gap in the balance of payments are also accepted.

The responsible attitude of the Trade Union movement in facing the nation's economic difficulties is also demonstrated by labor's continued voluntary acceptance of compulsory arbitration of industrial disputes, with the result that there have been no large-scale official strikes in industry since 1945. Although Communists exercise some minority influence in the trade union movement, there is a growing and active movement to eliminate Communists who exploit their trade union positions to undermine the European Recovery Program. The Annual Trades Union Congress Conference in 1948 administered a resounding defeat to all Communist-inspired resolutions introduced. Communists are excluded from membership in the Labor Party and there are only two Communists among the 640 members in the House of Commons.

The United Kingdom has traditionally one of the most stable governments in Europe. The Labor Government, which has been in power since 1945, still holds the commanding parliamentary majority which it won that year. Although in parliamentary byelections since 1945, Labor's electoral margins have declined, the Conservatives, the chief opposition party, have increased their representation in Parliament at the expense of Labor by only one seat. The next general election is scheduled for the spring of 1950; as this time approaches it can be expected that internal political and economic problems will take on increasing importance. Although the Conservatives are becoming increasingly critical of certain aspects of the Government's foreign policy, there is no basic conflict between Conservative and Labor in the broad field of foreign affairs, nor on the basic proposition that Britain's recovery depends on full participation in ERP.

2. Military Considerations Affecting Recovery

There is also basic agreement on defense matters. An emergency rearmament program was announced by the British in September. Plans are limited by a reduced power position and the continuing struggle for economic recovery. The program is designed to alert the country to the seriousness of the international situation, to furnish strength for emergency needs and to coordinate the defense establishment. Measures include postponement for 3 months of the release of conscriptees, intensive recruitment of regular and reserve forces, production of munitions and appreciable strengthening of the air arm. Although difficult to translate into precise economic terms the direct cost of the program will probably add on an annual basis roughly 200 million dollars to Britain's annual defense bill which was budgeted at 2.8 billion dollars for the 1948–49 budget year. There will be, in addition, indirect costs to industry. The central fact remains that the emergency defense program is limited in dimension and its cost can probably be absorbed within present economic margins without depressing consumption levels or disrupting investment or export plans.

Chapter II. Basic Problems of the British Economy

The discussions in the preceding sections of this analysis should by now have served to point up the immediate as well as the basic problems faced by the British economy, so they need only be raised here.

As has been made clear, political stability in the United Kingdom is marked and does not create a problem for recovery. There is fairly general agreement on ultimate goals, although there may be and are, disagreements on method. While there are inflationary factors present in the economy they have been contained and there is every prospect that the Government, which recognizes the elements of pressure in the economic situation, will continue to carry out policies designed to restrain inflationary tendencies and limit to moderate and supportable increments any rises which may be unavoidable.

An underlying problem for the United Kingdom in maintaining an acceptable level of domestic economic activity and standard of living is to overcome the loss of net invisible income which served to support production and consumption in the past. The two essential requirements to this end, increased domestic resources and increased payment resources to maintain the necessary flow of imports from abroad, depend on domestic investment to increase productive equipment, and on increased production and exports.

A basic problem of the British economy is therefore to achieve such increased levels of production and productivity as will allow the maintenance of a competitive position in world markets. For this purpose the country must devote a significant proportion of its resources to investment, and Government policy is directed to accomplish this end. Incentives to capital investment are apparently sufficient since the problem has been to restrain capital formation to the physical limits of material availabilities rather than to encourage it, except for specific industries.

Even higher levels of investment, in physical terms, than can be supported in the programs presented might be desirable as a means toward the increased productivity and production required. From a study of the allocation of resources among the various sectors of the economy, it hardly appears that domestic consumption could stand significant reductions for diversion to the investment program, and exports are necessary to assure the essential flow of supplies. While the estimate of the proportion of resources devoted to investment appears approximately correct, the over-all estimate of gross national product suggested in the presented material is so rounded as to cover considerable marginal variation, probably sufficient in most respects to provide for current levels of investment somewhat in excess of official estimates. The rate of investment will, however, continue to be subject to limitation due to general shortages of essential material components.

In view of the necessity for making the most efficient use of the resources to be devoted to investment, the suitability of the direction of investment must be examined. For instance, the United Kingdom has an excess of finishing capacity in the steel industry as compared with the domestic production of crude and semifinished steel. In the expanding economy, steel has been, and continues to be, critically short despite an extraordinarily successful effort to lift the level of domestic crude production. British coal mining is hindered by obsolete methods and equipment particularly in certain operations such as haulage and coal preparation where productivity is behind Continental and American achievement.

By the nature of these industries, long-term investment projects are required to overcome some of their deficiencies and it may take a very considerable period of time before the fruits of such investments can be realized in increased production capable of earning its way through a contribution to domestic supplies or exports. At the same time, it is clearly essential to lay a proper base capable of supporting the expanding level of the whole industrial complex.

Throughout the investment programs, consideration must be given to the element of relative cost since increased productivity must not be achieved at such levels of cost as will preclude maintenance of a competitive position in world markets. This is particularly a problem if the United Kingdom is to maintain or better its position in Western Hemisphere markets.

Beyond the adequacy of capital resources there are two elements bearing on the problem of continuing increases in production. The first is the continued shortage of certain essential materials, for example, steel and other metals, which may constitute a hindrance to attainment of a smooth flow of production. The second is the unlikelihood of any further increases in the labor force. Increased productivity per man-year and per man-hour appears to offer the only remedy to the long-range problem posed here.

While the Government has attempted to redirect labor from the less essential to the more essential industries, this program has certain obvious physical and political limits. In the first place, the shift can hardly be direct, since often a chain of shifts in employment might be required to accomplish, for example, an increase in labor employed in coal mining by a decrease in retail distribution. In any case in a democratic society compulsory redirection of labor has very distinct limits. Acceptable measures to achieve the most effective deployment of the labor force must be sought.

The United Kingdom, like other participants, must overcome its external deficit on current account and reduce its dollar deficit to manageable proportions. The drive for exports complements increasing production to this end.

In the pressure for exports to pay for imports and to prevent a further loss of reserves, the British have planned, with only very modest relaxations, to continue austerity at home. There is general responsible recognition of the difficult circumstances in which the United Kingdom finds itself and there would also appear to be a reasonable acceptance of the measures necessary to overcome the problem.

While austerity may be a temporary solution to the most efficient spending of resources in the international markets to assure the flow of essential materials and foodstuffs, it raises a question of effectiveness at home as well as a problem abroad. There is always the possibility that an increase in the availability of consumption goods might act as an incentive to increased effort and consequent increases in production. For this argument to be used effectively it must assume that the increase in production achieved will more than pay for the incentive goods, since increased levels of production in most instances require increased levels of supply.

The United Kingdom recognizes that it is to its own interest and to that of all participants that the levels of trade should be as high as possible, and if this is to occur it must mean an ultimate expansion over and above a mere exchange of essentials.

Although allocations of critical raw materials to industries are tied to production for export, there is no specific direction of exports by area. The official desire to increase exports to the Western Hemisphere is widely known and often repeated. The question arises whether the United Kingdom could not increase exports to the Western Hemisphere to a greater extent than is programmed. To the degree that nondollar markets are as profitable and more easily accessible to United Kingdom producers, they may tend to avoid the effort necessary to attain the maximum feasible exports to the Western Hemisphere and hard currency destinations. Marketing methods and techniques must also be improved to further the most effective pursuit of exports.

A nation may adjust its activities to unfavorable terms of trade, when they are known and continuous. Deteriorating terms, however, involve constantly increased efforts merely to stay in the same place even though they may, in some measure, appear to facilitate export programs. This has been the case for the United Kingdom in the recent past. Actually some United Kingdom bulk purchase contracts served to delay the impact of increases in world prices for imported commodities which might have resulted in even greater deterioration than statistics presently show.

Although it has taken an increasing volume of exports to pay for imports, up to the present time the United Kingdom has been able to sell everything that could be spared for export markets. Any pressure of disadvantageous comparative prices has consequently been so limited as to remain relatively ineffective. Since such a state of affairs cannot be expected to be permanent, account must be taken of the problem in planning for the future.

Chapter III. The United Kingdom Long-Term Recovery Program

A. CENTRAL OBJECTIVE AND BASIC POLICIES

1. Dollar Balance by 1952

The United Kingdom long-term program aims at an approximate dollar balance and a surplus on the order of 400 million dollars on current account over-all by the end of the ERP period.

This is to be accomplished by:

(1) Increases in total exports, and in exports to the Western Hemisphere;

(2) Increases in total imports to a maximum volume approximately 85 percent of prewar;

(3) Decreased imports from the Western Hemisphere;

(4) Increased domestic and colonial productive resources, and

(5) Increases in net invisible earnings.

It is hoped the remaining deficit with the Western Hemisphere will be of an order that can be met by use of gold and dollar earnings of the rest of the sterling area and the proceeds of commercial capital investment from the United States.

2. General Policies

The United Kingdom has called its long-term program submitted to OEEC a provisional draft contributed to the discussions from which a joint European Recovery Program is to emerge.

This program takes the same general approach to the problems of the economy that was outlined in chapter II. A general increase in productivity will be emphasized as the source of higher industrial and agricultural production. If projections are achieved over the four years an increase in personal consumption per capita above 1947 and in some respects above prewar should be possible. Improved supply of meat, eggs, oils, and fats should mean a better diet than in 1947 and 1948. Exports will hold primary place in planning. Capital investment will continue to take as large a part of the national product as the capacity of the British people to sustain austerity and the economy's need for export proceeds will permit. Fiscal policy will be directed toward maintenance of full employment and countering inflationary pressures. The particular form to be taken by successive budgets cannot be forecast at this time, but continuation of annual budgets designed to produce a surplus of revenue over current expenditure appears probable. Such action would help to counteract inflationary pressures, if a deficiency in voluntary saving in relation to the proposed level of investment seems likely.

Controls over home production and consumption will continue under scrutiny. The decontrol process is continuous and those controls retained are being simplified. Among the consumer goods at present rationed, a considerable number are likely to be freed as conditions improve under the recovery program, but the continuation of food rationing will probably be necessary for a somewhat longer period.

B. INCREASING PRODUCTION

1. Levels of Activity

A strong production effort provides the essential basis for other British program elements and substantially establishes the feasible levels of domestic consumption, investment, and export.

The British long-term program targets suggested for 1952–53 provide for expansion of output in manufacturing, mining, agriculture, building, and public utilities, taken as a whole, to a level about one-third above prewar. In spite of a constant or slightly declining labor force, increases in manufacturing output to a level of about 40 percent above 1938 are proposed. Production in the major segments of the British economy has still a considerable way to go to reach these goals.

2. Investments

The United Kingdom relies in its long-term program on a capital investment program taking approximately 20 percent of gross national product for fixed domestic investment and investment overseas to expand productive capacity. Fixed domestic investment is roughly estimated at about 8.5 billion dollars.

Projected gross ECA aid to the United Kingdom for 1948–49 is equivalent to 14 to 15 percent of this fixed domestic capital investment program. In subsequent years it is expected to be even less, but the strategic role of dollar aid is in financing dollar requirements essential to the progress of the whole economy.

Fuel and power, transport and communications, agriculture and industry constitute approximately 56 percent of the total domestic investment program (including housing maintenance and small projects). Most of the projects in these categories are direct parts of the recovery program. Some, such as power, transport, and industrial projects like refractory bricks, ball bearings, and precision chains, will contribute primarily to a general strengthening of the economy. Others, such as petroleum, coal, chemicals, shipping, agriculture, have a more direct bearing on the balance of payments.

The British program does not set a fixed upper limit to the amount of capital investment that may be undertaken. It is, however, limited broadly by the available supplies of critical materials, particularly steel. A fine balance must be struck in allocating steel in accordance with the requirements of the capital investment program, direct and indirect exports, home consumption and defense. According to the percentages given in Britain's long-term program, present allocations are roughly as follows:

	Finished steel (millions of gross tons)	Ingot equivalents [1] (millions of gross tons)
Capital investments (including maintenance and repairs)	6.7	9.1
Direct exports [2]	1.0	1.3
Indirect exports	2.6	3.5
Home consumption and defense	.9	1.2
Total	11.2	15.1

[1] Based on 1.33 conversion factor.
[2] According to OEEC definitions—does not include products such as wire and tabular goods.

These figures indicate the small part of the steel supply going to consumption and defense, and the bulk of the supply already going to capital formation. A 10 percent expansion of investment would take the major part of the consumption and defense uses. On the other hand, a 10 percent reduction in consumption and defense, even if it could be obtained, would release only minor quantities for investment use. A significant expansion of supplies for investment necessarily would have to come out of exports.

There is little reason to suppose that any substantial expansion of investment at the expense of exports is feasible within the present limits of ECA assistance and the need to achieve dollar and over-all balance by 1952. The possibility, however, remains that substantial diversion of steel from investment to defense uses may become necessary.

3. Agriculture

Britain's long-term agricultural program is designed to provide more food for the increased population without increasing import expenditures. Home production of food is to increase about 15 percent over present levels to yield one-third more in calories for human consumption than prewar. However, the United Kingdom will still remain the world's largest importer of food.

Success of the over-all program depends to a considerable extent upon mechanized operation. As a result of the present high degree of mechanization, a transformation in British agriculture largely brought about during the war, soils which had previously been too heavy for efficient manual cultivation are now being effectively worked and produce good yields. Supplies for further mechanization and modernization will probably be made available since the farm machinery and equipment industry at the end of 1948 was producing at seven times its prewar rate and keeping up with deliveries to domestic farms despite heavy exports. Imports of farm machinery are limited to types or sizes not produced economically in the United Kingdom at the present time. By 1952, however, the British expect to produce all types of farm equipment with the exception of a few special items like extra heavy crawler tractors.

The agricultural program also includes a further increase in the use of fertilizer, improved farm credit facilities, expanded research and educational projects, the payment of modest subsidies for initial drainage of lands, and other activities in support of the goals.

Cropping projects are also to be supplemented by increased livestock production, so that beef, veal, and egg production will be above prewar; sheep and hog production, however, though higher than at present will still be less than prewar.

The British propose to carry on the whole agricultural program with a rise of only 10 percent in the farm labor force over 1938. Although efforts to attract new agricultural labor have not been as successful as desired, this year's crops were harvested without serious loss. Farm labor requirements may therefore turn out to be less than estimated after the full impact of the mechanization program has been felt.

Total capital investment required to modernize and mechanize the existing plant and expand to the goals set out is equivalent to about 1.8 billion dollars. This is only three and one-half times the estimated annual value of saved imports, so the program if achieved may pay for itself in terms of foreign exchange savings. Prices guaranteed to British farmers are comparable to the costs of commodities bought elsewhere and imported into Britain.

Success of the British agricultural program depends on many factors, e. g., estimates of the future cost of imported food supplies, the uncertainty of supplies from foreign sources, and the likelihood of markets being found for a sufficient volume of British exports to pay for more food imports than are called for under the present plans.

C. EXPORTS

1. The Export Drive

The long-term program establishes an export target for 1952–53 of 150 percent of 1938 volume. Such levels had been closely approached toward the end of 1948.

The production of sufficient goods to meet and maintain the overall export target will, as previously stated, require a substantial physical improvement in industrial output, and continued restrictions on home consumption. Foreign demand, however, may prove a more severe limitation.

The British have become increasingly conscious of the marketing problem to be faced in maintaining the level of exports required to finance the necessary level of imports. The present program is a readjustment of earlier estimates that maintenance of approximately the prewar volume of imports would require a volume of exports at least 75 percent above the 1938 level. The program as now formulated represents, therefore, a fundamental change of policy, largely based on a reappraisal of world markets for British exports. If world trade should increase beyond the levels currently assumed, British exports might also share in the general increase.

The danger in such a situation as faces the British is that the administratively simpler attack of controlling imports may tend to outweigh emphasis on the necessity for concerted and strenuous efforts to further exports.

The problem is more complex where the object is not only to increase the total level of exports, but to increase the volume of trade in areas where competition is most keen. Under present conditions, the whole structure of trade arrangements may tend to limit incentives to the individual exporter to push exports to the difficult hard currency areas. Export targets established for the end of the recovery period are, however, according to the British program, based on "a realistic assessment of probable trends" and represent "in no sense maximum" quantities. The program further states that "if sales opportunities allow, British policy will be adapted to achieve a higher level."

The degree to which exports may overcome the dollar deficit may be of greater importance to the solution of the present problem than the over-all total. Immediately before the war the United Kingdom sold about 4.5 percent of total exports to the United States and 17.5 percent to the Western Hemisphere as a whole. The object of the program is to increase these proportions to 6 and 20 percent by 1952–53. Since the total volume would be greater, this would mean an increase in shipments to the Western Hemisphere of about 80 percent over the volume in 1938.

United Kingdom exports to non-Western Hemisphere areas are also expected to rise more than 40 percent above prewar. The export drive is, therefore, not only aimed at the dollar gap but extends to all major world markets.

Relations with other participating countries are of primary interest to ERP. Before the war participating countries took approximately one-quarter of Britain's exports. The British long-term program projections suggest that in 1952–53 they will take about one-fifth. Since the total volume of United Kingdom exports is to be increased by 50 percent, even this decreased proportion will, in fact, mean an increase of 20 percent in shipments to the OEEC countries as compared with the 1938 level.

The exports of the United Kingdom to the other participants must still be analyzed in relation to the total trade of these countries with the sterling area.

United Kingdom postwar trade with Eastern Europe is far below the prewar level, but is slowly increasing. The long-term program assumed revival and reasonable expansion of trade with Eastern Europe.

2. Export Targets—External Factors

Realization of exports depends on more than plans to export without other implementation. Even allocation of resources to favor exports by production, investment, and fiscal policy and controls, however, cannot assure the maximum volume of export sales. The cost of production and consequent selling prices will be a factor of major and increasing importance. These elements are only in part subject to British control.

Other factors beyond the control of Britain are rising competition from the rest of the world, political and economic instability in various areas, and the restrictive trade practices which tend to accompany instability.

The sellers' market of the immediate postwar is showing signs of limitation as the demand for some types of goods is satisfied. Certain unusual export markets which Britain now has for products in the dollar area, such as automobiles, for example, may be considerably narrowed. The quality and price of British goods, granted the ability and willingness of the Western Hemisphere countries to buy, are the basic factors that will enable Britain to meet or exceed Western Hemisphere export targets.

3. Marketing Methods

Increasing interest in the possibilities of stimulating foreign demand through progressive selling methods is developing in Britain. It is agreed that the success of the export drive in helping to close the dollar gap may depend to a considerable extent on more general use of modern and progressive marketing techniques.

Trade promotion of individual products will be left to private industry, and suggestions are being solicited from importers of British goods in the United States. The Board of Trade, however, has offered to cooperate with private industry in matters of general interest. The British Government at the present time permits the use of dollar exchange for advertising purposes if reasonably satisfied of a return in increased sales of British products in dollar areas. The whole field of market development calls for thorough exploration through systematic research to determine possibilities for expanded sales, to discover what British products, not presently imported by the Western Hemisphere, have a potential market there, and to determine which British industries might expand production to meet the needs of newly discovered markets.

D. IMPORTS

1. General Import Policy

British import policy generally is aimed at the most economical use of resources to buy the goods needed to continue the drive toward ERP objectives. This involves curtailment of some types of imports and shifts in source for others. Food consumption will be maintained by an expansion of production within the United Kingdom itself. According to British estimates, domestic production before the war provided the nation with only about one-third of its food. By 1952–53, British agriculture is expected to supply between 55 percent and 60 percent of the nation's requirements. Since food and food imports made up one-half of Britain's total imports in 1938, the importance of these plans is clear. Imports of raw materials and petroleum, essential to the attainment of the production goals set in the long-term program, will be slightly higher than before the war, but less essential items are to be strictly limited.

2. Import Program With Respect to Areas

Unless the flow of imports into the Western Hemisphere countries from the United Kingdom can be greatly increased, the approximate dollar balance of 1952–53 will be too limited to allow unrestricted dollar imports. The material limits to this policy, dictated by the need to maintain an acceptable standard of living at home and supply the necessary raw materials for industry, are apparent. If dollar earnings can be increased over projections, there will be room for increased dollar purchases.

Imports into Britain from areas outside the Western Hemisphere, taken as a whole, are expected to approximate prewar volume, but will be restricted in the interests of the over-all balance of payments.

The United Kingdom is being criticized by some of the other participants for not buying more freely from them. This derives from the problem of expending limited British resources most effectively and the necessity to economize on nonessentials. The repercussions of restriction may, however, affect achievement of export targets.

The give and take needed to meet this problem is a factor in the intra-European payments plan, and it is stated British policy to work out with debtor countries arrangements for increased total levels of trade in both essentials and nonessentials.

E. PROJECTED BALANCE OF PAYMENTS

1. General *

The British project a net surplus on current overseas account for 1952–53 of 400 million dollars, and a deficit on current dollar account just under 300 million dollars.

The success of the long-term program of the United Kingdom will depend upon the achievement of projected export and import targets, as well as upon the degree to which the planned shifts in trade patterns are accomplished.

Within the over-all targets the United Kingdom hopes to increase exports to the Western Hemisphere and particularly to the dollar area above the target figures, while at the same time decreasing imports from these areas. Planned imports from areas outside the Western Hemisphere would have to increase relative to imports from hard currency areas.

Despite the limited import program, the projection made for 1952–53 assumes a deficit on merchandise account of 600 to 700 million dollars.

By 1952–53 the British hope to have restored or even surpassed the prewar level of net earnings on invisible account. The chief elements in the improvement are expected to be the oil industry and shipping revenues.

Government expenditure overseas and travel will mean net outpayments. Although the British hope to double the prewar level of tourist receipts, British tourist spending is expected to increase and result in a higher deficit than prewar.

Although gross returns on foreign investment are expected by the British to be substantial in 1952, the United Kingdom has so greatly increased its own indebtedness that net receipts from interest, profits, and dividends are expected to be only a fraction of prewar.

Within the net surplus projected on current account, there is a traditional surplus with the sterling area, with which close commercial and political relations have been maintained. Before the war the United Kingdom had an adverse merchandise balance with this group of countries, but earnings on invisibles sufficient to yield a very substantial 1938 surplus. The prewar surpluses with the sterling area could be used by the United Kingdom to balance its traditional deficits with the Western Hemisphere and Europe. After a wartime lapse from this pattern which resulted in increased sterling balances held by the sterling area, the United Kingdom is again earning a surplus in this area and expects to continue to do so. In 1952–53 the surplus with the sterling area is projected by the British at 800 million dollars.

Britain customarily incurred a deficit with the other participating countries in prewar years; for 1952–53, present British drafts suggest a net surplus balance with the nonsterling participants of approximately 50 million dollars.

The approximate balance which is projected in the Western Hemisphere calls for 1952–53 imports slightly below the levels of 1948 and projected exports about 80 percent above the 1938 volume. The British, however, feel that this estimate is not only realistic in terms of their own goals but that it also allows for considerable Western Hemisphere absorption of imports from other participating countries. The deficit with the Western Hemisphere of about 300 million dollars is at a level which can be met by the gold production and dollar earnings of the rest of the sterling area if, as is now customary, these hard currencies go to balance the United Kingdom surplus with the area. The British projection of payments with various currency areas in 1952–53 must be considered in the framework of the interrelated character of European and of world trade, fitting the United Kingdom elements into a pattern with the participants, the rest of the sterling area, and other nondollar countries. If the United Kingdom achieves its projected surplus with the other participants, these countries will have to earn sterling to pay in return. This might be achieved in areas where the United Kingdom has a deficit, or by exporting to sterling area destinations.

There is still another aspect of the pattern of trade that requires consideration. Before the war there were, in addition to Ireland, certain other European participants, which relied on converting sterling earnings to meet their needs in other currencies, especially dollars. The approximate or manageable dollar position estimated in the long-term program does not allow apparent leeway for a large volume of such conversions.

F. OVERSEAS DEVELOPMENT PROGRAM

The British recovery program includes plans for the development of resources, including world-short strategic materials, in overseas territories.

British colonies and other dependent territories have considerable untapped resources awaiting development. Those economies are basically agricultural and to a lesser extent depend on mining. They are likely to remain predominantly dependent on the extractive industries for a considerable period of time. Further developments in colonial areas will depend in many instances on expanded transportation facilities. The British Government has allocated $116 million for expenditure by 1956 for civil aviation, ports, harbors, railways, roads and telecommunication. Important among other steps is the preliminary survey being undertaken for a new rail link to join South and Central Africa with the East African railway system. United States technical assistance for such a survey was requested and approved by the ECA Administrator. In addition the government is engaged in projects with the local colonial governments for the topographic and geologic mapping of colonial areas and other fundamental research. The United States is assisting in some of these projects.

Basic British legislative provision for colonial development was provided by the Colonial Development and Welfare Acts, which as amended in 1945 established a credit of 480 million dollars to be expended during the decade from April 1, 1946, to March 31, 1956. Under these acts, 17 of the 45 eligible territories have submitted 10-year development plans involving a total expenditure of 720 million dollars. About 240 million dollars of this total is chargeable against the colonial development and welfare fund; the balance is to be provided from colonial revenues, reserves, and loans.

In February 1948 the Overseas Resources Development Act was passed providing for the establishment of two public corporations—the Colonial Development Corporation and the Overseas Food Corporation with total resources of 440 million and 220 million dollars, respectively, to carry out development projects. On the basis of investment by Government, semipublic, and private sources, the colonial contribution to European recovery should be significantly enlarged.

G. EXTERNAL ASSETS AND LIABILITIES

1. Gold and Dollar Reserves

The British maintenance of sterling as an international currency is given in the long-term program as a major objective requiring corollary maintenance of gold and dollar reserves against further depletion during the period of ERP. Most of the sterling area countries rely almost wholly upon the United Kingdom and the sterling area mechanism for meeting their dollar deficits, since their own foreign exchange has been maintained traditionally in sterling.

In the effort to prevent further drain on reserves, the British have reduced their own dollar imports, and have called upon the other sterling area countries to do the same, with some success.

During the war, the sterling obligations of the United Kingdom increased greatly, the total mounting to more than 14 billion dollars. The sterling area and certain other countries, which could not be paid in commodities or services, accepted sterling balances in repayment. Although there have been some reductions since the end of the war, through "unrequited" British exports supplied against these sterling balances and by conversion into dollars, the balances outstanding remain high and represent a problem to be faced.

Whether gold and dollar reserves can be maintained throughout the three remaining years of the program depends, of course, upon whether ECA allotments are sufficient to cover the diminishing dollar deficit. If long-term recovery is to take place, the speed with which this deficit can be reduced is limited by the level of imports necessary to sustain the economy while the capital investment program is being carried out.

The British program makes no provision for increasing gold and dollar reserves during the recovery period. The balance of payments projected for 1952–53 suggests that Britain's earnings of gold and dollars from the sterling area will all be required to finance the remaining dollar deficit. The prospect is, therefore, that despite strenuous efforts, the United Kingdom will not find it possible to increase reserves to any substantial degree by 1952–53, nor in the early years thereafter.

Chapter IV. The Second Annual Program, 1949–50

A. INTRODUCTION

For the program-year 1948–49 the amount of ECA financial assistance proposed for the United Kingdom is 1,239 million dollars. Part of this gross aid is being extended conditionally, dependent upon extension of aid by the United Kingdom to the other participating countries. Under the intra-European payments plan, the United Kingdom is making net drawing rights of 290 million dollars [1] available to the other participants. (See allocation of aid funds for 1948–49, chapter I for detailed discussion.)

The program submitted by the United Kingdom for the year 1949–50 estimates the amount of financial assistance needed from the United States as 940 million dollars. This amount of gross aid is about three-quarters of that granted by ECA in 1948–49. While the program for 1949–50 envisages steady progress in the expansion and reorganization of all key economic activities, the projected rate of expansion is less pronounced than actual performance in the recent past. This, to a degree, is a reflection of the fact that some consolidation of the substantial gains already made will occur in order to provide a sound basis for subsequent improvements. It may also reflect recognition that, with total production and export rates already so markedly above prewar, and with available labor now fully employed, the gains from here on must come almost entirely as a result of the effort to increase productivity—both per man-hour and per man-year. One of the main factors contributing to this increased output per worker will be capital investment leading toward further mechanization and modernization of industry.

The level of economic activity as a whole is slated to rise during 1949–50 to a point 30 to 35 percent above prewar compared with an estimated 25 to 30 percent by mid-1949. Production going to the home market and production for export are to remain in about the same proportion to each other. Total volume of exports is put at 145 percent of 1938, as against a planned 137 percent for 1948–49. Total

[1] Subject to final OEEC approval of 8 million dollars agreed to with Turkey.

imports are to be held down to about the same level as in 1948–49, in line with the general program of supporting the economy with decreased dependence on overseas resources. The volume of imports has not yet returned to prewar levels and the object is to keep it about 15 percent below prewar. Consumer living standards will be raised only in a most limited way and then only if production has been increased sufficiently to permit it. Investment will continue to absorb about 20 percent of the gross national product. It should be remembered throughout that the United Kingdom assumed as a limit in programing that total dollar outlays should not exceed current resources including aid and credit.

No precise estimate of either side of the national resources balance sheet is possible, since the magnitudes of the components which make up the totals on either side can be, at best, only illustrative forecasts. It has nevertheless seemed feasible to analyze the problem, and the proposed solutions to it with some confidence in the general findings.

B. SOURCES OF RESOURCES

1. Production

Domestic production is expected to average 30 to 35 percent higher than prewar, and the table below, submitted by the United Kingdom to the OEEC, indicates the stage of activity in various industrial sectors of the economy.

Progress in key segments of United Kingdom economy in year 1949–50, as compared with prewar; 1947, 1948–49 and 1952–53 goals

	Prewar	1947	1948–49	1949–50	1952–53
Grain production	4.6	6 3	7 6	8 0	8.4
Meat and bacon output	1.5	.9	.95	1.05	1.5
Milk output (including milk products)	7.3	8.0	8.0	8.4	9 0
Solid fuel output [1]	254.0	223 0	244.0	256.0	286 0
Electric power output	21.3	42 6	45.0	46 5	55 0
Oil refined	2.6	3 1	5.1	6 1	16.8
Steel output	11.4	12.7	15.0	15.5	17 0
Copper used	266.0	356 0	381.0	385.0	427.0
Timber consumption	12 6	6.3	6.7	7.0	7.7
Textile production index	100 0	75 0	92.0	100 0	104.0

[1] Of which the following figures are for coal: Prewar, 233.0; 1947, 201.0; 1948–49, 218 0; 1949–50, 230.0; 1952–53, 257.0

All figures in million metric tons, except electric power output (billion kilowatt-hours), and copper (thousand metric tons), timber (in million cubic meters of sawn timber, excluding sleepers) and textile production (index of raw material consumption). Prewar figures are for 1935–38, except for milk and milk products 1936–38, other foodstuffs 1934–38.

a. Coal.—It was hoped by the United Kingdom that in 1949–50 coal output would rise by 12 million metric tons to 230 million from the 218 million estimated for 1948–49. On this basis, solid fuel exports of 27 million metric tons would be possible (coal, 26 million tons and coke, 1 million tons). Since deep-mined production has lagged in 1948 (about 2½ million tons below the calendar year target), the

British export estimate for 1949–50 has already been reduced by 1 million tons. On the basis of current performance, therefore, 1949–50 production targets, nominally unchanged, are probably too optimistic.

The British hope to attain the proposed level of production, partly by measures of rationalization, such as concentration of output in more efficient collieries and the more productive sections of individual collieries, and partly as a direct result of the capital expenditure incurred during earlier years.

For 1949–50, as for 1948–49, reliance must be placed mainly on short-term developments, of which there will be several hundred designed to produce an early increase of output or reduction in costs by means of mechanization underground, the reorganization of haulage methods, and the development of drift mining. Some of the new cleaning plants already ordered will also be coming into operation during this period. In the fiscal year 1949–50, a further 135 million dollars is expected to be spent but even certain of the short-term developments will not, in fact, be completed and producing their full results during the year. Every effort is being made to expedite their completion so as to get results at the earliest possible date.

b. Steel.—The United Kingdom estimated that during 1949–50, blast-furnace capacity for steel making pig iron would be increased by half a million tons as a result of the investment program and that a total of 7.7 million tons of pig iron for steel making would be produced. Production of steel ingots and castings is also to increase during the next few years by an estimated 500,000 tons each year. The program for 1949–50 suggests production of 15.5 million tons ingot equivalent compared with a 1948 target of 14.7 million metric tons and actual production approximately 400,000 tons higher. The crude steel target is predicated on the assumption that adequate supplies of imported scrap and rich iron ore will be available. If European demand for these materials continues to increase, both may continue in short supply. The rates of production actually achieved during 1948, however, suggest the possibility that the 1949–50 production target also may be substantially exceeded.

Blast-furnace and steel-making facilities are reported operating at capacity level, and imports of semifinished steel during 1949–50 will be a substantial aid in employing finishing capacity that might otherwise remain underused. Exports of finished steel are expected to be somewhat higher than the 1948–49 program of 1.2 million tons.[2]

Despite the rapid expansion of domestic production, lack of steel is still one of the major limiting factors in the recovery program. If more steel were available both the capital investment and the export programs could be accelerated.

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[2] OEEC definitions of steel products.

c. The engineering industries.—The over-all investment program in the United Kingdom is expected to consume about $2.6 billion in plant, machinery and vehicles, during 1949–50. Thus, domestic consumption of the production of machinery industries will provide for expanding and modernizing industrial and agricultural processes and make an indirect as well as a direct contribution to subsequently increased exports.

Examples of the rise in the scale of effort in 1949–50 which, even under the handicap of insufficient steel, the machinery industries will bring to bear on dollar saving and on export earnings are shown in the following tables supplied by the British:

Production 1949–50 in the machinery industries—estimated increases in output compared with 1948–49

Wheeled tractors	10 percent (100 percent in sizes over 40 horsepower).
Crawler tractors	150 percent (new production building up).
Power plant	15 percent.
Automatic looms	10 percent.
Hosiery machinery	New and rising supply of machines especially destined to meet the lay-out of small factories.
Machine tools	Start of production on types for which United Kingdom has previously relied on imports from dollar and other sources.
Chemical plant	20 percent.
Steel and non-ferrous metal manufacturing equipment.	Approximately 20 percent.
Ball bearings	10 percent.
Enameled wire	50 percent.
Contractors' plant	15 percent increase in exports.
Coal-face machinery	30 percent increase in exports.

The forecast increases are for the most part comparatively moderate and with capital investment as planned it is expected that goals set for these industries will be attained.

Substantial quantities of the indicated increased production are scheduled to go to meet the equipment needs of other participating countries, and of the sterling area as well as the rehabilitation of United Kingdom industry itself. The success of the production drive in these industries will largely depend on the attainment of projected steel availabilities.

The table above indicates the important role played by the machinery industries in the export drive, and suggests that in 1949–50 this contribution to recovery will remain proportionately the same, even with the expanded total export targets.

d. Shipbuilding.—Shipbuilding is a major industry in the United Kingdom. The yards today have a greater volume of work in

Forecast of production for export in the United Kingdom machinery industries

[Expressed as a percentage of total production]

	Mechanical machinery	Electrical machinery and electrical goods	Road and rail vehicles	All machinery
Average	33.6	19.6	37.5	31.3
Mid-1948 average	36.5	22.9	48.1	37.3
Mid-1949	40.0	23.5	50.0	41.0
Mid-1950	40.0	23.5	50.0	41.0

hand than at any time in the past quarter of a century. The principal problem confronting the industry is a lack of materials, especially steel. However, despite complaints of steel hunger and allocation stringency, the industry is expected to meet its 1949–50 targets. New construction for United Kingdom register, assuming minimum allowances for obsolescence, should bring the mid-1950 dry cargo tonnage figure up to 12.8 million gross tons and the tanker tonnage to about 13.8 million gross tons. The tanker program accounts for almost 46 percent of ship tonnage now on order. Most of the building now under way consists of passenger vessels, cargo liners, and tankers. Very few tramp steamers are being built.

e. Textiles.—If plans for increasing the production of textiles and steering a larger proportion of the output into export markets are realized, the consumption of raw cotton in 1949–50 could be expected to rise by one-third over 1947 and wool by about one-fifth. While there was continuous improvement in production in the calendar year 1948, the targets, taking the industry as a whole, were not met. The 1949–50 targets propose to lift production to prewar levels. In the light of current lagging performance, meeting textile targets will require a rapid and vigorous attack upon problems of manpower recruitment and redeployment, increasing efficiency of operation and modernization of equipment. 1949–50 should see the coming into operation of new nylon and rayon plants, and the outlook in this sector of the textile industry should be somewhat more favorable.

f. Agriculture.—Plans for agricultural production in 1949–50 call for increased acreage of staple crops and an improved livestock program. Average plans suggested in a few major groups are: Bread grains, 11 percent above the present year's program though 28 percent below the peak year of 1943–44; feed grains, 6 percent above 19498–49 and 7 percent above 1943–44; potato acreage is expected to fall, which is consistent with larger supplies of other foods becoming available; sugar beets, a slight decrease to the long-term level. Examination of the generally expected yields discloses that the additional lands being brought into cultivation are not marginal producers but are expected to yield as well as lands cultivated prewar. On the basis of the yield and the price paid to obtain the increased output, the 1949–50 crop program would in general appear feasible of attainment. Bread grain seedings in the fall of 1948, however, have not come up to acreage seeded in the fall of 1947.

Special stress is given to increasing animal numbers toward prewar levels and to improving the grassland for livestock. The quantity of animal feeds available next year will obviously not affect the meat production in 1949–50, but increased quantities should make it possible for animal numbers and eventually production to go up.

Since meat production depends principally on food supplies made available over the last 2 or more years and on known grass conditions, the 1949–50 program should be a reasonably sound estimate. The following table illustrates that, except in the case of milk, production of principal livestock products in 1949–50 will remain substantially below prewar.

Index numbers of total production of livestock products in the United Kingdom

[Prewar average=100]

Commodity	Prewar average [1]	1946–47	1948–49	1949–50
Milk	100	106	110	114
Meat:				
Beef and veal	100	93	86	90
Mutton and lamb	100	71	57	63
Pig meat	100	33	37	48

[1] Average farm years for 1936–39.

The heavy losses of sheep and cattle in the floods and blizzards early in 1947 will involve smaller output of beef, veal, mutton, and lamb in 1949–50 than 1946–47, just as it does in 1948–49.

2. Imports

For 1949–50, as for 1948–49, the United Kingdom plans for a volume of imports approximately 85 percent of prewar. The submission to OEEC was designed to provide the raw materials and equipment and the petroleum products considered necessary for the steady maintenance of industrial and agricultural production, development, and modernization in accordance with the over-all programs. The proportion of the import program devoted to industrial raw materials and production supplies was expected to increase as a result of increased food supplies from domestic production. The forecast food import program may be considered merely adequate to the limited consumption goals and, in some segments, serious doubt exists as to even this degree of adequacy. Planned imports of industrial raw materials, although well over half the import program seemed no more than sufficient to sustain the scheduled increases in industrial production. Although significant reductions in the volume of the raw materials segment of the import program are probably directly prejudicial to achievement of production goals, it has already been necessary to plan for smaller imports of nonferrous metals in view of continued world shortages. ECA screening of the British import program in terms of availabilities and requirements suggested some revisions of the original estimates but these have no significant effect on total imports. The estimate of dollar import requirements submitted by the United Kingdom was found to be conservative.

C. USE OF RESOURCES

1. Personal Consumption

The drive for exports and the restriction of imports force Britain to maintain substantially her present austere standard of living. Present fiscal policy is to channel a large part of British production away from home consumption and into exports and the improvement of British plants. Improvements for the consumer remain a residual claim on total resources.

Austerity, however, cannot be carried too far or continued too long. The British public has been subjected to severe limitations on consumption ever since the beginning of World War II. It is British policy to increase when possible the amount of certain consumer goods, especially clothing and certain kinds of foods, and to restore the general level of food consumption above abnormally low levels imposed after the financial crisis of 1947.

The level of food consumption in 1949–50 will be about the same quantitatively as 1948–49, but there may be improvements in quality by increases of about 5 percent over the 1948–49 consumption of meat, bacon, and milk. Supplies of sugar may also improve and it may be possible to increase egg consumption, present rations being one egg per week.

In 1948–49 the estimated average per capita per day consumption of 2,900 calories was still below the prewar level of 2,950 calories. While this may under present conditions be regarded as a relatively adequate caloric level, plans of the United Kingdom for 1949–50 and subsequent years, which would about maintain this caloric level, are reasonable only if they concentrate upon improving the quality and variety of the United Kingdom diet. Despite the increase in sugar consumption, the expected average for 1949–50 is still about 20 percent below the prewar level. Meat consumption, if meat contracts are successfully negotiated and with increased domestic slaughter, may rise in 1949–50, compared with the current fiscal year, which was lower than expected because of import short-falls. However, 1949–50 will still be about 25 percent below prewar. Limited world availabilites restrict a more rapid recovery of meat and fats consumption to prewar levels. Efforts to increase fish and milk consumption will continue.

A decrease in potato production in 1949–50 is expected to cut per capita consumption from 130 kilograms per capita in 1948–49 to 120 kilograms in 1949–50. This will mean a decided improvement in the United Kingdom diet, since quality foods, high in nutritive content and variety, will begin to replace the bread and potato diet. Rationing of meat, bacon, fats, eggs, cheese, sugar is expected to continue throughout the coming year. Controls at distribution levels will still be necessary for grain, milk, and many canned food products in extremely short supply.

ECA analysis suggests the following illustrative comparison of food consumption:

United Kingdom—preliminary food consumption Estimates for 1949–50, based on ECA screened import program

	Prewar	1948–49	1949–50
	Kilograms per capita per year		
Grain as flour	95	119	117
Sugar, refined [1]	49	38	38
Potatoes	79	130	120
Dry legumes	3	3	4
Vegetables	55	63	63
Fruits and nuts	60	54	55
Meat	65	44	47
Fish	24	35	35
Eggs	11	9	9
Whole milk	126	153	155
Cheese (fat content)	4	3	4
Fats (fat content)	21	18	18
	Calories per person per day		
Total	2,950	2,900	2,900

[1] Including sugar content of glucose.

2. Government Consumption

Various public statements of British officials suggest that approximately the present level of total Government consumption is assumed throughout the 4-year program, although there may be some offsetting changes in the components. Concerted effort is being made to keep expenditure in the Government consumption sector to a minimum. If anything beyond the presently planned moderate increase in military expenditures is budgeted for in the future, it will require a revision of the national income estimates all along the line.

A moderate increase in the use of resources in the Government sector of the economy may even be possible out of what appears to be a probable excess of gross national product over conservative estimates, without disrupting the programs for capital formation, exports, or personal consumption.

3. Capital Investment

The proposed investment program for 1949–50 is a key element in the whole recovery effort. Total gross investment on new buildings and plants, and on the repair and maintenance of existing capital equipment were estimated roundly by the United Kingdom at 8 billion dollars, given as equivalent to about 20 percent of gross national product. As indicated, the proportion may be approximately correct, but a higher magnitude of value does not seem unlikely with a more detailed estimate of gross national product. This additional capital will be the most important new factor helping the United Kingdom to produce and earn enough gradually to restore the prewar standard of living for an increased population and, at the same time, to balance external accounts. Since the labor force is now fully deployed, and shortages of labor are likely to develop within the program year, most of the increased output on which the United Kingdom depends will have to come from increased output per worker. The program is thus especially dependent upon increased investment as a means of raising the productivity of labor.

The investment program for 1949–50 gives special emphasis to finishing quickly those projects already started and to beginning as soon as possible other projects which will help to end basic shortages affecting production, or will make direct savings of imports.

The limiting factors to investment in 1949–50 are more likely to be physical than financial. Shortages of some basic materials, notably steel, affects practically every kind of investment and will overshadow financial limitations to investment. For every 7 tons of steel required for home investment in 1949–50 only about 6 tons can be provided. Despite rigid economies in use and the large steel investment program, demands for exports as well as for home investment are so large that there is no prospect of any significant easing of the shortage before the end of 1950. This checks the rate at which investment may be increased in the oil, coal, electricity, railway, and shipbuilding industries. Besides steel, shortage of softwood (nearly all of which must be imported, some from dollar sources) and of cement, will also affect investment programs. Apart from these physical factors the local shortage of building labor, especially skilled labor, in some areas where many large investment projects are in hand, and the imperative need for expanding exports of machinery and equipment (now contributing over 20 percent of all exports) also impedes the rapid expansion of investment.

About half of gross investment, estimated in the neighborhood of 4 billion dollars per year, is required to cover the depreciation of capital assets. Only the balance, or net investment, is available for the expansion of productive capital as well as to make up wartime damage and to provide housing for the increased population. The areas to which the investment program will be devoted are suggested in the following table:

Gross ivestment in main segments of the United Knigdom economy including housing maintenance and miscellaneous small projects for year 1949–50

	Percent
Fuel and power	12
Transport and communication	14
Agriculture	5
Industry (including iron and steel and shipbuilding)	25
Housing	21
Essential social services	5
Administration and defense	4
Miscellaneous	14

a. Investment in key industries—Coal.—In 1949–50 the long-term program for the reconstruction of the mines will still be in its early stages and no very great increase in the rate of progress can be expected. One hundred thirty-five million dollars is expected to be spent on development and reconstruction, plant replacement, and new coal preparation plant, but much of this will not affect production in 1949–50. Productivity in deep-mined coal is, however, expected to increase about 5 percent over 1948–49. Just as in 1948–49, reliance must be placed during the 1949–50 period largely on short-term developments, and on the direct result of capital expenditure incurred during earlier years.

Petroleum.—Total investment in petroleum development during 1949–50 will be about 500 million dollars, nearly 400 million dollars of which will be for expenditures on overseas production, maintenance, and new construction, and 100 million dollars to 120 million dollars of which will go toward expanding refinery capacity in the United Kingdom itself.

One large new refinery is planned in the South of England, and the capacity of a number of existing installations is to be expanded considerably. The substantial overseas investment involves projects to increase the production of refineries in the Middle East, the Caribbean, and in Holland, some of which are already under way. Rehabilitation work will be continued on the war-damaged refineries and oil fields in the Far East.

Iron and steel.—Recognizing the limiting effects of the steel shortage, Britain gives high priority to the vital expansion of steel capacity. Capital expenditure on building and plant during 1949–50 will be about 150 million dollars (excluding about 19 million dollars to be expended in dollars in the United States, mainly for progress payments on steel plant equipment, some of which will be delivered during the year). Blast-furnace capacity for steel-making pig iron will be increased by half a million tons. The expansion program includes finishing mills, but the primary emphasis will be on schemes to increase crude-steel capacity in order more nearly to balance available finishing capacity and reduce shortage-created hindrances to production, and the most effective use of plant.

New capacity for the production of billets and wire rods will come into operation during the year and will tend to ease import requirements for semifinished steel and wire rods. The new hot-strip mill in South Wales should be in partial operation by the end of 1949–50, although the cold-mill and tin-plate facilities probably will not be in production for at least another year.

The full development at Corby Northamptonshire will raise steelmaking capacity by about 700,000 ingot tons a year; 140,000 tons of this is expected to come into operation in 1949–50. Associated with this will be the development of ore-quarrying equipment and ore-preparation plant, coke ovens, blast furnaces, steel-making plant, new billet mills, and the reconstruction of primary rolling mills.

The construction of new batteries for coke will be supplemented by schemes for economy in the use of fuel by the greater use of coke-oven gas.

Although the developments described in the previous paragraphs are important in themselves, the year 1949–50 remains primarily a period of construction and work in progress for the industry, and it is estimated that over 17,000 building workers will be engaged on construction work.

Agriculture.—It is anticipated that a substantial part of the new investment required for expanding the annual output of British agriculture to meet the targets set by the long-range program will have taken place by the end of 1949–50. Modernization of existing plant will continue throughout the 4-year period, and an increasing proportion of expenditure will go to repair and maintenance. Total expenditure in 1949–50 will be about 360 million to 400 million dollars. About 6 million dollars of this will go toward buildings for agriculture, education, and advisory work of various kinds, and the balance of new investment and replacement will provide increasing numbers of the more modern types of machinery. Productivity is, therefore, expected to increase.

Engineering industries.—The products of these vehicles and machinery-making industries continue to constitute a dominant part of the export program and provide the means of expansion of industrial and agricultural processes in the United Kingdom. Effort will, therefore, to a great extent in order to save imports, be focused on those particular industries in this group which can make the products essential to the maintenance, modernization, and expansion of the total industrial plant of the country and which will also provide larger quantities of these products for export.

Electricity.—Particularly important in connection with the plans for increasing industrial output and productivity is the proposed 1949–50 investment of 400 to 500 million dollars in electric generating plants, transmission lines, and distribution systems. This would be about one-fourth of the investment envisioned by the long-term plan to increase generating capacity approximately 50 percent above the present level by 1952. The need for greatly increased supplies of power is well recognized as a key prerequisite to the installation of modern industrial plant and technique. The Anglo-American Council on Productivity has stressed this point.

During the year 1949–50, it is estimated that 1,600,000 kilowatts additional generating capacity will become available in the United Kingdom. This is the largest increment for the 4-year period (1948–52) as planned, and results from the completion of projects laid down prior to the start of the European Recovery Program.

Shipping.—Investment in new-ship construction in 1949–50 will constitute a further implementation of the program already well under way to restore Britain's position in ocean-going tonnage of dry-cargo vessels and tankers. The projections made in the second annual program, raising the merchant fleet to 12.8 million gross tons dry cargo and 3.8 million gross tons in tankers, seem attainable. In fact, as the load of repairs and reconversions becomes lighter, new construction may increase, bringing tonnage for United Kingdom register somewhat beyond the level now planned for mid-1950.

The British dry-cargo fleet is still about 1.7 million gross tons below the 1939 level. The tanker fleet, however, has now reached a tonnage half a million above the prewar level.

Textiles.—Investment programs for the textile trades are part of the long-term program for reequipment of spinning and weaving facilities, reorganization, and recruitment. A considerable volume of work will be done in 1949–50. Mechanization of weaving has been limited by availability of looms and only about 20 percent of the goal for 1952 will be installed during 1949–50. Additional synthetic capacity, especially in staple fibers and nylon yarn, will come into production during the year.

4. Exports

The 1949–50 program calls for exports at an average volume for the year equivalent to 145 percent of prewar. This would be an increase of approximately 6 percent over the projection for 1948–49 and approaches the long-term export goal of 150 percent of prewar volume.

The program proposes to increase exports to the Western Hemisphere by approximately 15 percent above 1948–49, which, as planned, is to be 45 percent above 1947. The 1949–50 target requires that almost 18 percent of total exports be absorbed by the Western Hemisphere, with the United States taking about one-quarter, Canada and Newfoundland another quarter, and South and Central America the remaining half. Increases in exports to the dollar areas of the Western Hemisphere already have been substantial. While there may be some adjustment among the various dollar destinations, it does not, from the evidence now on hand, appear likely that total dollar exports will exceed the projection significantly during the period.

Export goals depend first on achievement of production targets supported by the planned level of imports, especially in essential metals, and second on meeting competition on quality and price. The United Kingdom is on the whole meeting her current export-volume targets and may even be able to exceed them.

D. THE INTERNAL BALANCE OF FINANCE

For the year 1949–50, the economic program implies little in the way of major changes in inflationary pressures despite a projected decrease in the general balance of payments deficit from a present estimate of approximately less than three-quarter billion dollars for 1948–49 to an estimate for 1949–50 approximately one-third lower. If investment in the United Kingdom is in fact progressing during the current year (1948–49) at a level somewhat higher than had been projected originally, as appears reasonably clear, then the investment program for 1949–50, if literally adhered to, would seem to imply a drop in total investment which would more than cancel out the decrease in use of overseas resources. If, on the other hand, the investment program approximates the current levels, as seems more likely, the increase in inflationary pressure is negligible. On the favorable side, furthermore, there is the anticipation of increased production and rising national income, which should not only yield increases in personal and business savings but rising revenues as well.

In any event, considering the effective manner in which the Government has responded to fluctuating inflationary pressures heretofore, any that can now be foreseen cannot be regarded as a serious threat to the United Kingdom economic recovery. This does not imply any recent relaxation of inflationary pressure; there has been mild pressure, and upward movements in prices and wages have resulted, but these have been moderate and have not disrupted progress toward the major objectives of British economic recovery.

There is no doubt that the carefully planned fiscal policies of the United Kingdom are being used effectively to promote financial stability.

E. THE BALANCE OF RESOURCES

If statements in the United Kingdom program which imply a direct relationship to the level of gross national product in 1949–50 are taken at surface value, an estimate not much higher than actual in 1948 results. This would not be entirely consistent with other data at hand. While the index of industrial production showed signs of leveling off in the spring, after the rapid rise of the last few years, activity again increased in the fall of 1948. The estimated 2 to 3 percent annual rate of expansion of the gross national product throughout the ERP period is roughly consistent with various statements in the 1949–50 and other programs about industrial manufacturing and agricultural output, and the level of economic activity. Since the labor force is now fully deployed, most of this increased output will have to come from increased labor productivity. Direct evidence on the current rate of increase of productivity is inconclusive; but, in the light of "normal" prewar rates of increase and of the concentrated efforts in the United Kingdom to increase the supply of capital, reduce absenteeism, increase know-how, etc., the projected rate of increase of gross national product seems to be attainable. As already noted, this expansion of output will probably proceed from a higher initial level for 1948 than that suggested in the broad estimates quoted by the two annual programs for the ERP period which have thus far been submitted.

With these qualifications in mind, estimates of the distribution of resources have been prepared and set out below. As indicated, in an expanding economy with increasing national product, an increased proportion of resources may reasonably be programed for investment.

Distribution of available resources; 1949–50, (1948 prices)

[In billions of dollars]

	Assumption A	Assumption B
Resources available:		
Gross national product	$43.0	$43.3
Index (1948=100)	103.8	104.5
Resources from overseas (net)	$0.5	$0.5
Resources available for home use	$43.5	$43.8
Index (1948=100)	103.3	104.0
Gross domestic investment	$8.0	$9.3
Percent distribution	18.4	21.2
Index (1948=100)	92.5	106.9
Allocation of resources:		
Government consumption	$7.7	$7.8
Percent distribution	17.7	17.8
Index (1948=100)	100.0	101.3
Personal consumption	$27.8	$26.7
Percent distribution	63.9	61.0
Index (1948=100)	107.8	103.8

In presenting the picture of resources available and their distribution, the table has been prepared on 2 sets of assumptions. A, attempting to present the national accounts as closely as possible to official statements and estimates, B, alternatives are set out which are in some cases more realistic and in some instances merely more desirable. Thus in A, GNP is shown increasing at an annual rate of 2½ percent, while in B the rate is assumed to be 3 percent. The element of foreign borrowing is the same in both tables and is taken from present estimates. Government consumption is kept stable in table A at the 1948 rate, while in table B a rise of $100 million per year is estimated for 1949-50. In both projections, A and B, personal consumption is derived as a residual. Base for the index comparisons, 1948, is estimated.

While this table exhibits possible variations in estimates and in policies—such as the division of resources between consumption and investment—both sets of assumptions result in substantial agreement on points of basic importance. First, the rise in gross national product will be sufficient to overcome the declining use of net foreign resources and still make available for home use an increased volume of goods and services. Secondly, both show that a large proportion of these resources can be devoted to modernizing the economy without compelling a decline in personal consumption.

These magnitudes have important bearings on the problem of inflation and, if fulfilled, should mean some easing of pressure. Under A, based more closely upon official estimates, the pressure from modernization and rebuilding will become progressively smaller. Even under the more ambitious program set up in B, which results in a minor rise in the proportion of resources abstracted for investment, this may be less than a possible rise in savings as income rises.

ERP aid, in this balance, constitutes in quantitative terms only a small fraction, about 2 percent in 1949–50, of the total resources which will be available to the economy.

Such a comparison, however, cannot show the critical role of ERP assistance, for the lack of which the basic magnitudes, such as the increase in the gross national product, would have to be revised downward. This in turn, would affect all other magnitudes, such as investment and consumption.

F. BALANCE OF PAYMENTS

The foreign trade presently estimated as necessary in 1949–50 to implement British recovery plans for production and domestic use of goods and services will result, on current assumptions as to other relevant factors, in a balance of payments deficit on current account of approximately one-half billion dollars (including trade with British dependent territories). This over-all deficit represents a substantial step forward from the deficit of more than 2.5 billion dollars in 1947.

Despite the deficit on total account, there is a net surplus on non-dollar account, a substantial surplus with the sterling area in effect overcoming the net excess of payments on current account with other participants and other nonparticipants outside the Western Hemisphere.

Anticipation of increased supplies from the other participants results in a shift from the estimated surpluses on United Kingdom account during the first half of 1948 and as estimated for 1948–49 to a deficit in 1949–50. The position of the other participants against sterling, however, must be determined by their relationship not only with the United Kingdom but with the whole of the sterling area. On present estimates, it would appear that assistance in the framework of the intra-European payments plan may require a substantial net grant of drawing rights by the United Kingdom.

1. Dollar Accounts

The current deficit on dollar account is now estimated somewhat in excess of 1 billion dollars for 1949–50. The submitted program relied very heavily on substitutions of non-Western Hemisphere sources for the import program. On the basis of current performance and informed estimates of availabilities, it did not seem probable that import surpluses of the magnitude programed with these areas outside the Western Hemisphere could in fact be realized.

The status of the current account is, however, an inadequate accounting of the sum of dollar obligations which must be considered in order to determine the prospective total requirement for gold and dollar settlements and the appropriate level of aid. As in the 1948–49 program, some adjustment must be made for the so-called capital account items which must be met on a current basis; for example, amortization payments on dollar debts with the United States, settlement payments of gold and dollars to countries outside the dollar area, prospective net receipts from the dollar earnings of the rest of the sterling area outside of the United Kingdom, and for other credits and income.

In 1949–50, the dependent overseas territories and the rest of the sterling area combined will on balance earn dollars for the United Kingdom at a rate that is expected to result in a net dollar surplus. This compares quite favorably with an approximate balance projected for 1948–49 and results, in part, through increased earnings from the dependent overseas territories, which will be expected to have recovered the arrears of the war and, in part, through continued import restraint by the independent sterling-area countries, whose continuing shortage of capital equipment suggests that to anticipate still further decreases in the dollar deficit on their account may be overoptimistic.

In addition to these, there are, as described previously, net settlements resulting from balances on payments agreements with other countries. Although payments of this type with other participating countries are currently running at a very substantial rate, the principal allowance made on this account for 1949–50 is to meet part of the Western Hemisphere deficit of the Netherlands West Indies, which is customarily provided for by the United Kingdom because of dollar requirements for petroleum-trade operations in that area. Should the swing of balances necessitate gold or dollar payments to other participants in 1949–50, as they have in 1948–49 despite the operation of the intra-European payments plan, and current funds be insufficient to meet the drain, it may be necessary to review the recommendations on the level of aid.

While there are elements in the net settlements with other nonparticipants which, as in the 1948–49 program, are not considered by the United States in making its calculations of aid, they do require dollars and must be taken into account in considering the effect of the program in relation to reserves and other resources.

From the screening of trade estimates and examinations of other features of the dollar accounts, the balance requiring extraordinary financing would appear to have been conservatively estimated by the United Kingdom and the total requirement would now appear to be in excess of the original projection.

In estimating requirements for aid, the United Kingdom assumed, on its own responsibility, that the Canadian Government would allow drawings on the remaining balance of the Canadian credit at the rate of 10 million dollars per month. An allowance for such drawings has been included among receipts, reducing the requirement still remaining to be financed. The resumption of drawings at this rate was announced January 21, 1949.

G. DOLLAR AID RECOMMENDATIONS

On a summary of the estimated current and capital account balances, the total deficit on dollar account is somewhat less than 1 billion dollars.

The British program submitted to OEEC requested an allotment of 940 million dollars and this is the amount which ECA believes necessary. It is recognized that this is not sufficient to cover total dollar requirements as presently estimated, even allowing for the deduction of elements which it is believed would be more suitably financed otherwise. If undue recourse to reserves becomes necessary the Administrator may find it desirable to review this recommendation.

This conclusion may be supported by the following summary of program considerations:

The British request for assistance is an attempt to forecast needs on the basis of (1) realistic appraisals of capabilities, and (2) minimum requirements which cannot be satisfied from Britain's own resources.

The second annual program can be described as a carefully considered step along the road to viability. The sharp upward trend in the production and export curves which has characterized the recent past should tend to flatten out somewhat during 1949–50 as the natural result of the ending of the period of redeployment of productive resources from wartime to peacetime uses. The year should still see significant gains in the reorganization and expansion of key productive activities upon which the United Kingdom depends for attainment of 1952 goals under ERP and consolidation of the improvement which will have taken place by the middle of 1949. Many key projects of industrial development will be moving toward completion and Britain's industrial plant by June 1950 should be in a far better position to tackle the ambitious targets to be maintained under the long-term program.

While the full effect of progress in 1949–50 will not emerge fully until the later stages of the 4-year effort, the ability of the United Kingdom to put sufficient resources into the reconstruction of her production plant in 1949–50 will, to a significant extent, determine these results.

Sufficient assistance in 1949–50 is therefore vital to the success of the long-term recovery program.

The assistance requested of ECA is 940 million dollars. The amount of gross aid requested is therefore less than three-quarters of that granted in 1948–49.

When account is taken of the net drawing rights that will probably have to be extended under the intra-European payments plan, the allowance of net aid for direct use by the United Kingdom may be substantially less.

With the support of ECA aid, the total import program as planned offers every reasonable evidence of British concentration on the recovery objective. It forms, when added to domestically produced resources, an appropriate link in the merging of all elements of total national resources available to do the job. Its magnitude appears in general to be adequate, with practiced economy, to the task assigned.

PART III

Appendix Tables

ILLUSTRATIVE BALANCE OF PAYMENTS TABLES FOR 1948–49 AND 1949–50

TABLE 1.—*Illustrative balance of payments for 1948–49*

[OEEC estimate in millions of dollars]

	Dollar account			Non-dollar account	Grand total [1]
	United States	Other	Total		
1 Imports	699	943	1,642	5,374	7,016
2 Exports	281	441	722	4,873	5,595
3. Merchandise balance	−418	−502	−920	−501	−1,421
4. Invisibles (net) [2]	+64	−249	−185	+497	+312
5. Current account balance	−354	−751	−1,105	−4	−1,109
6. Settlements	+42	−194	−152		
7. Capital transactions:					
(a) Non-ECA financing		+66	+66		
(b) Repayments	−50	−22	−72		
(c) Other					
8. Net position	−362	−901	−1,263		
9. Estimated requirements for United States aid			1,263		

[1] Total excludes trade with own dependencies
[2] Invisibles on nondollar and total account derived. No submission data for parts of the invisible account.

TABLE 2.—*Illustrative balance of payments for 1948–49*

[ECA estimate, in millions of dollars]

	Dollar account			Non-dollar account	Grand total [1]
	United States	Other	Total		
1. Imports	742.2	885.7	1,627.9	5,329.2	6,957.1
2. Exports	281.0	441.0	722.0	5,016.0	5,738.0
3. Merchandise balance	−461.2	−444.7	−905.9	−313.2	−1,219.1
4. Invisibles (net)	+64.0	−249.0	−185.0	+712.0	+527.0
5. Current account balance	−397.2	−693.7	−1,090.9	+398.8	−692.1
6 Settlements	+42.0	−244.0	−202.0		
7. Capital transactions:					
(a) Non-ECA financing	+10.0	+66.0	+76.0		
(b) Repayments	−50.0	−22.0	−72.0		
(c) Other					
8. Net position	−395.2	−893.7	−1,288.9		
9. Estimated requirements for United States aid			1,239.0		
10. Uncovered deficit			49.9		

[1] Excludes trade with own dependencies.

TABLE 3.—*Illustrative balance of payments for 1949–50*

[United Kingdom estimate, in millions of dollars]

	Dollar account			Non-dollar account	Grand total [1]
	United States	Other	Total		
1. Imports	776	850	1,626	5,647	7,273
2. Exports	285	495	780	5,124	5,904
3. Merchandise balance	−491	−355	−846	−523	−1,369
4. Invisibles (net)	+82	−202	−120	+658	+538
5. Current account balance	−409	−557	−966	+135	−831
6. Settlements	+122	−163	−41		
7. Capital transactions:					
(a) Non-ECA financing		+132	+132		
(b) Repayments	−48	−17	−65		
(c) Other					
8. Net position	−335	−605	−940		
9. Estimated requirements for United States aid			940		

[1] Excludes trade with own dependencies.

TABLE 4.—*Illustrative balance of payments for 1949–50*

[ECA estimate, in millions of dollars]

	Dollar account			Non-dollar account	Grand total [1]
	United States	Other	Total		
1. Imports	836.3	826.5	1,662.8	5,500.4	7,163.2
2. Exports	285 0	495.0	780.0	5,332 0	6,112.0
3. Merchandise balance	−551.3	−331.5	−882.8	−168 4	−1,051.2
4. Invisibles (net)	+82 0	−202.0	−120.0	+658.0	+538.0
5. Current account balance	−469.3	−533.5	−1002.8	+489.6	−513.2
6. Settlements	+122.0	−173.0	−51.0		
7. Capital transactions:					
(a) Non-ECA financing	+15.0	+132.0	+147.0		
(b) Repayments	−48 0	−17.0	−65.0		
(c) Other					
8. Net position	−380.3	−591.5	−971.8		
9. Estimated requirements for United States aid			940.0		
10. Uncovered deficit			31.8		

[1] Excludes trade with own dependencies.

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