

ECONOMIC EMERGENCY MEASURES FOR THE TRANSITION PERIOD.*

by Eugene V. Rostow

I

Our international economic relations are in a state of deepening crisis which threatens the peace. The emergency in our foreign economic policy is as great in scale, and as menacing to American security interests, as the financial emergency which preceded the passage of the Lend-Lease Act. We now lack an adequate program for achieving freedom of the exchanges, and for financing the export of American supplies during the emergency period after German surrender. Without such a program we cannot realistically expect to reach one of the first great goals of our national interest--the restoration of a large volume of international trade, conducted on the basis of free and stable exchanges and lowered trade barriers.

The countries of Europe will end the war in differing economic and financial circumstances. Some, like the Soviet Union, will face fifteen years of rebuilding before the physical destruction of war can be replaced. Greece, Italy, Poland and Yugoslavia will be in a desperate condition of physical devastation and economic disorganization. Others may have suffered relatively little war damage, but will have to begin again with demoralized industries and finances, and depleted reserves of foreign exchange. For each country of Europe, even including the relatively rich countries like the Netherlands and Belgium, the transition years present serious problems of physical reconstruction, and of economic and financial planning. Every country of Europe will need substantial financial assistance to overcome obstacles created by the war, before it can undertake to re-enter a world economy based on free exchanges and liberal principles of commerce. The United States, Canada and the other countries of this hemisphere have not suffered the physical impact of the war. They alone will have surplus supplies to make available at its conclusion. Assistance in supply and finances must come to Europe primarily from the West.

Europe will need American supplies, if reconstruction is to be quick and real, but no European country will be able for several years to export enough goods, or to provide enough services, to pay for them currently. Yet we have no credit arrangements for financing the export of supplies needed for the economic reconstruction of liberated areas. We have no policy beyond the wartime limits of our lend-lease program for financing the reconstruction needs of Britain and the Soviet Union. As a result of the absence of American credits, liberation has proved to be an economic shock to France, Italy and Belgium. For Britain and the Soviet Union, the tapering off of our present lend-lease war programs at the end of the war with Germany will be an even greater and more dangerous shock. We have not developed the policy or the procedures which can fill the gap.

*This paper is scheduled to appear, in a shortened form, in the January issue of Fortune magazine.

A review of existing legal resources tells the story. The Johnson Act blocks one possible form of reconstruction financing, the inadequate powers of the Export-Import Bank another. Although from the strictly legal point of view the Lend-Lease Act offers much, the policy which has so far governed its administration makes it doubtful whether that powerful and flexible weapon will be used with sufficient drive to meet the needs of the emergency situation. UNRRA can deal only with the civilian relief requirements of Eastern Europe, which have been very narrowly defined. It is expressly forbidden to undertake reconstruction activities. The constructive measures proposed at the Bretton Woods Conference have not yet been approved by the Congress, and in any event they will not go into effect for a considerable period of time. They are not intended to meet the needs of the emergency directly ahead, and at best they can deal only with a small segment of the problem of reconstruction.

At the Bretton Woods Conference last summer, great progress was made towards setting up arrangements to assure freedom of exchanges and a considerable flow of investment capital in the second phase of the post war adjustment.

But the International Monetary Fund proposed at Bretton Woods is not intended to provide facilities for relief and reconstruction, or to deal with international indebtedness arising out of the war. Its resources cannot be used to finance the unfreezing of currencies. The draft Agreement for the Fund contemplates that in the countries most directly affected by the war exchange restrictions may well last at least three years after the Fund begins its operations, and permits no action against such restrictions for at least five years after the Fund begins operations. The basic policies of the Fund of course require the progressive relaxation of exchange restrictions, and call for penalties against their unwarranted continuance. But the Fund does not of itself provide the machinery nor the resources to assure their liquidation. That preliminary step must be accomplished by other means.

The Bank for Reconstruction and Development, proposed at Bretton Woods, is designed to assist in the restoration of economies destroyed or disrupted by war, and in bringing about a smooth transition from a wartime to a peacetime economy. A part of its \$10 billion lending authority can be used to facilitate the financing of specific projects of reconstruction, at rates of interest which will give special consideration to the needs of borrowers who have suffered devastation. Such loans can be made, after the Bank is organized and in operation (not before May 1, 1945, at the earliest, and probably not for many months after that date), only after each project has been formally reported on by a committee, and if the Bank is satisfied that the loan could not otherwise have been obtained on conditions reasonable to the borrower. The Bank is an institution of great promise, greatly needed. But its lending power is hedged about with limitations which may well prove serious. Its charter has overtones of excessive orthodoxy. And it will be a year at least before any reconstruction loans can be placed even within the eligibility limitations of the Bank's rules. In fact, a year is a most optimistic estimate of the time which may be required before loans are placed. The UNRRA proposal, infinitely less controversial and less complicated than the Bretton Woods plans for a Fund and a Bank, required more than six months to be approved by the Congress, even after the UNRRA agreement was signed. The Bretton Woods proposals will not be signed for several months. After that, they face a new Congress, with the handicap of announced opposition by the crucial group of cooperative and internationally minded Republicans who have so far supported

the Administration on every important issue of foreign policy. And they face also the announced and determined opposition of some important members of the banking community. Yet the next year will be the critical and decisive time during which new patterns and directions for European life will be established. We cannot afford to be passive watchers of that process.

The dangers to security interests of the United States implicit in the current crisis of international supply can only be compared to those of the war itself. Our economic policy during the next five years can cement the association of the United Nations, or it can destroy any real hope of security or stability in their political and military arrangements. We can help powerfully to strengthen the forces of progressive and democratic government in Europe, or we can let popular government in Europe go down, without our economic support, before extremism and reaction. We have a good chance to bring about the reestablishment of a system, generally speaking, of free exchanges and multilateral trade for the capitalist part of the world. That system would be the best possible foundation for a world order in which our safety as a nation, and as a democratic society, might be cheaply and collectively secured. It would constitute the best and mutually the most profitable basis on which our close and friendly relations with the Soviet Union can be maintained and developed. Indeed it is doubtful whether peaceful political relations can be securely built on the foundation of an economic system using the methods of barter, controlled exchanges, and bilateral trade. So far as we have known such methods only as forms of economic warfare, or as instruments of political warfare.

The danger is that unless the United States establishes adequate emergency credit facilities at once, and on an appropriate scale, the world will drift into an economy of blocs and groups. Extreme forms of protection, restriction and bilateral trade arrangements exist. If they continue, they will split the capitalist part of the world down the middle. Such developments would go far to wreck the political and military unity on which we depend to prevent a third German war. They would force us to establish exaggerated state controls over our own economic activities, and require an indefinite continuance of certain wartime measures of mobilization. Manifestly, such trends would have most unpleasant implications for our domestic way of life.

It takes no argument to prove the advantages which accrue from the system of triangular trade. Those advantages are both economic and political. On the economic side multilateral trade methods are essential if the volume of world trade is to become large enough to play its part in the general strategy of full employment. They are essential too if our potentialities for increased economic welfare are not to be frittered away in subsidized, protected and wasteful forms of barter. As the largest economic unit in the world, we have the most to gain from a restoration of world trade on a multilateral basis. Our memory is too fresh of the Germans forcing the Turks to exchange chrome for German harmonicas to confuse bilateral trade methods with economic progress. The political advantages of multilateral trade are even more obvious, and more urgent. Bilateral trade methods require cumbersome domestic economic controls. They make every economic transaction a direct political responsibility of government. They increase the instability of economic life, and multiply the opportunities for political friction and bickering among friendly peoples. It would be hard to conceive a plan more directly designed to divide the United Nations than to translate all trade among them from the commercial to the political and governmental plane.

Our failure to act as the world's chief banker for the transition period may well lead to a hopeless freezing of the postwar world, in economic patterns which would menace the possibilities of peace, by the time the Bretton Woods plans are intended to go into full operation. Emergency measures have a way of creating vested interests, which then prove difficult or impossible to liquidate. If general exchange controls, government monopolies of foreign trade, barter trade practices, quotas and other direct wartime economic control practices survive the war for five years, the purposes of the Bretton Woods conference may well prove impossible of realization. The continuance of such controls for any extended period after the surrender of Germany will reduce our chances of achieving full employment at home. They will inevitably lead to political friction among the Allies, and to counter measures on a serious and threatening scale.

II

The starting point in any program for the transition period is the future of our economic relations with Great Britain. The course of our dealings with Britain will largely determine how we trade with France, the other countries of western and central Europe, Australia and New Zealand, Africa and the Middle East. For in differing degree, they all suffer from the same prospect of a temporary but acute shortage of dollars which is plaguing the British. And their political associations, in the absence of a positive American policy, will lead them to economic coalition.

At the present time, Britain is operating in the world markets under a far-reaching and effective system of exchange control. Sterling is blocked, and most of the current dollar accruals of the entire sterling area are in effect sold to the British Treasury for sterling, to be available for war purposes. Thus if an Australian exporter sells some zinc, for example, to our United States Commercial Corporation for dollars, he is finally paid in Australian pounds, the Australian Treasury receives British pounds, and the British Treasury holds the purchase price in dollars. The British Treasury makes dollars available to the participants in this pool as the occasion may require. Its interest, of course, is to keep the dollar expenditures of the sterling area to a minimum. This policy we have strongly supported, as a necessary corollary of the lend-lease program. Faced with material shortages at home, and with the cost of financing lend-lease exports, it has been our constant policy to keep lend-lease calls on the U.S. to a practicable minimum, and to require Britain to be supplied where possible from a sterling source. The organization of a dollar pool for the sterling area was a highly desirable step in mobilizing all possible British resources of foreign exchange.

The virtues of this system as a war measure have been greatly proved in practice. Its menace in peacetime is equally apparent, as we move from a period of short supplies, distributed by governmental license and allocation, to one of ample supplies, distributed by the ordinary process of sale on the market. Picture an American exporter after the war, freed of WPB controls, trying to sell a car or a typewriter in Australia or the Belgian Congo. During the war, of course, the rule has been that American supplies would be sought only if the minimal approved need could not be met from a sterling source. Suppose the same rule, or an adaptation of it, were to apply in peace as a measure for conserving dollars, the one commodity of which all Europeans will

be short for some time after the war. The customer will tell the exporter politely that he would of course much prefer the American car or typewriter, but that his Treasury has unfortunately turned down his application for a license to pay dollars for it. He has therefore sadly placed his order for a machine of British, French or Belgian manufacture. The American exporter, in a rage, will appeal to the American Consul, to the State Department, the Treasury, and finally to his Congressman or to the Chicago Tribune. Long before the mysteries of foreign exchange can be explained to the public at large, there will be a hue and cry against the wicked and ungrateful British, who will be accused of outsmarting our diplomats again, after we have won the war for them.

The prospects of international bickering, bitterness and political reaction implicit in the maintenance of these controls are endless. Without their prompt liquidation, commerce in the immediate postwar period will be an affair of political negotiation and divided markets, not of competition between private interests. Exchange control is a far more powerful weapon of protection than tariffs, quotas, or barter deals. Unless we act to prevent it, however, we shall see such controls used on a wide and dangerous scale, and we shall face the consequences of international misunderstanding and disunity.

For the plain fact is that if the war ended tomorrow, Britain could not afford to unblock sterling, even for current transactions, or to give up her other controls of foreign exchange and imports, and no British politician could today take responsibility for proposing to do so.

The course of the war has borne heavily on British finances. While a part of the wartime disequilibrium in the British balance of payments has been met by lend-lease in the U.S., and by governmental gifts in Canada, the British have been incurring huge debts for war supplies and services in Egypt, India, the Middle East generally and in certain other parts of the world. British holdings of dollars have gone up, because we prefer to purchase the pounds we need for the pay of our troops, and do not accept them as reverse lend-lease. But the over-all condition of British finances is now worse than it was in 1941, and it is deteriorating with every passing month. The British will emerge from the war the only one of the Allies burdened with external war debts, and their indebtedness will be on a very large scale. It will reach \$12 billion at the end of this year, without any reference to supplies received as lend-lease in the U.S., or mutual aid in Canada, and the level is rising rapidly.* These figures do not tell the whole story. A large part of British war expenditures abroad have been met by the sale of securities, a measure which has permanently cut down what was formerly an important source of income on Britain's international account.

In face of their high level of short-term international debt, their loss of overseas investments, and the uncertainties which confront British export trade, shipping, aviation, banking, and insurance in the postwar world, the British are naturally concerned, indeed almost obsessed, with the future of their balance of international payments. Some students have concluded that the British balance of payments cannot balance for several years after the war. These studies underestimate the possibilities of British postwar trade with Europe, and of British penetration into markets formerly held by Germany.

*Interview with Lord Keynes. New York Times, July 7, 1944, p. 9, col. 1.

And like all guesses about the postwar world, they depend on what one assumes will be the general rate of economic activity, particularly in the United States. A careful economist estimates that if the United States maintains domestic employment at a level corresponding to a national income of \$150 billion a year, American imports will be from \$4 to \$5 billion more per year than before the war. The ultimate effect on world trade of such a policy may be an expansion of \$15 to \$20 billion, of which the British share would inevitably be very large. Yet the British themselves are afraid, in the light of present prospects, that at the end of the war they will not be able to unfreeze existing sterling balances, or to abandon exchange controls, and other measures for controlling the balance of payments. It would be difficult to dispute the British position, however one estimates the future possibilities of British trade, unless some way is found to deal with the blocked sterling claims representing war expenditures, presently held in Egypt, India, the Argentine, and other countries.

On the other hand, the British are determined to have full employment, social security, and economic progress at home after the war. Such a course will require a high level of imports, both in food and in raw materials, and it will tend to make British exports expensive, by keeping domestic price levels high. The accumulated needs of domestic consumers who have been without supplies for five years already, and the necessities of repairing the devastation of air raids in Britain, will put further obstacles in the path of cheap British production for export. Yet Britain must make great efforts to regain and enlarge her export trade, for the British know that only through an expansion of their international commerce can they make up for the wartime loss of their investments, and other overseas income, and thus pay in the future for the imports of food and raw materials they need to restore and improve their domestic standard of living.

The British may pursue these economic goals in one of two ways. The first would be to undertake their program of full employment and social development within the framework of a basic policy of free exchanges, competition and multilateral trade. The sterling balances now held by India, Egypt and other countries might be funded, in part, or released for gradual liquidation. But postwar transactions in sterling would be free. The second would be to continue with exchange controls, and with bilateral and preferential trade arrangements. Either course, intelligently pursued, could assure full employment at home, and the other imperative social goals of the British people.

The debate on the broad lines of British foreign economic policy after the war has given rise to violent controversy in Britain. On one side are the men who would prefer to keep wartime controls over external trade the shortest possible time, and return as soon as possible to an economic system of free exchanges and liberalized rules of commerce. The chief advocates of this view represent the dominant groups in British public life today--the Prime Minister, the Foreign Office and the Treasury. Their view will probably remain dominant unless we make such a program impossible of realization, through our failure to reduce our tariffs and to make adequate credits available.

The other side of the debate views the extraordinary battery of British wartime controls over external trade not as a necessary and temporary evil, but as a positive instrument of economic policy for the indefinite future. They are men both of the right and the left, and their preference for a system of highly developed state economic controls is both ideological and practical.

Lord Beaverbrook is one spokesman of this group. The influential Economist, usually a voice of the purest Manchester liberalism, has lately become another. Many mistake this type of wartime economic controls for the legal machinery required in a modern capitalist community to assure full employment and economic progress. Acting in concert, using their combined power to increase the flow of investment, at home and abroad, and to make the organization of business more competitive, Britain and the United States can together achieve a democratic program of full employment and economic progress. For fullest success, such a program requires common action in the international field to assure free and stable exchanges, and lowered trade barriers, the foundation stones of the largest possible volume of useful trade. But the ambiguities of the term "planning" have confused the real issues. The wartime methods in the field of inter-national economic relations--government purchasing, exchange controls, and the like--are not the key techniques for a program of full employment. In most forms, they do not represent economic progress, but only old autarchy, mercantilism and reaction, writ large in new and dangerous forms. The present tone of the debate indicates that this series of problems may well become one of the great rallying points for the controversies of the British party system.

A policy of state-controlled trade, based on licensed exchange transactions, bilateral commerce and extensive preferences, is one which Britain would be well equipped to pursue. She will emerge from the war relatively stronger in Europe than she has been in this century. Her factories will be full of modern equipment, she will have a high level of productivity, and enhanced political prestige and drive. Britain has great economic strength, though her international finances are now shaky. She could manage a program of restricted and directed trade, for some time at least, with relative success. In such a policy she might well gain the support and cooperation of other areas similarly situated financially, or politically affiliated with her, like France, Belgium, the Netherlands, Scandinavia, Italy, Spain, Portugal, Greece, Turkey, and Western Germany, the whole of Africa, most of the Middle East, the Dominions, and certain of the Latin American Republics. The world would be divided into separate currency and trade areas, which might easily become rival, not complementary to each other.

Such a policy of restrictionism on the part of Britain would be a disaster, both to our long-term interests and to her own. If current transactions in sterling remain frozen for any period of time after the war, a fissure will develop in the capitalist side of the world which will greatly weaken the foundations of its unity. It is not too much to say that our agreement with Britain and the other western democracies on the broad lines of a liberal monetary and commercial policy is the essential condition precedent to realizing our larger political postwar aims. The best hope for the security and prosperity of both countries requires a fulfillment of the economic pledges of the Atlantic Charter, and of Article VII of the Master Lend-Lease Agreement between the two countries--an undertaking which we have now entered into with most of the countries receiving lend-lease aid.

Article VII of the Lend-Lease Agreements calls for a lend-lease settlement whose terms and conditions will not burden commerce but actively promote an expansion of production, employment and trade, the elimination of "all forms of discriminatory treatment in international commerce," and the reduction of tariffs and other trade barriers. Of this Article the President has said: "If the promise of the peace is to be fulfilled, a large volume of production and trade

among nations must be restored and sustained. This trade must be solidly founded on stable exchange relationships and liberal principles of commerce. The lend-lease settlement will rest on a specific and detailed program for achieving these ends, which are, as Article VII of the agreements with Great Britain, China and Russia point out, 'the material foundations of the liberty and welfare of all peoples.'**

Clearly, the lend-lease agreements look to a liberal and multilateral, and not a restrictionist approach to the solution of world economic problems. But they are broad agreements of principle. They require mutual and reciprocal action if they are to become realities. The action on our part needed to carry out the policy of these agreements is on a much larger scale, and a much broader front than has so far been publicly indicated to be likely. There is a real danger that we shall fail to carry out the pledges of Article VII. Indeed, some steps so far taken or indicated, notably the proposed Oil Treaty with Great Britain and the kind of commodity agreements indicated as being under consideration, are steps in the direction of nullifying its principles and purposes. A continuance of the present crisis in our emergency supply relations with Europe may so fortify the institutions of restriction as to prevent us ever from reaching larger questions of commercial policy, such as the future of cartels, the level of tariffs and other trade barriers, and the abolition of preferences and quotas. Unless we devise a form of emergency financial aid which will make it possible for wartime control practices to be given up promptly at the end of the war, they are going to continue, and to spread. The momentum and the cumulative quality of restrictionism, as we saw in the period between wars, is great, and hard to overcome. The end of hostilities will give us a great but fleeting opportunity to start fresh. Later will be altogether too late.

It cannot be repeated too often that our financial arrangements must not be patchwork to conceal a basic lack of balance in our trade. We need to provide emergency credits in order to tide over the acute period of readjustment immediately after the war. But those emergency credits will be wasted unless we undertake at the same time to correct the fundamental error of our economic foreign policy since 1921--that we have been stubbornly, insistently, and vehemently trying to sell without buying. The British have held their system of imperial preferences in reserve, in all discussions of postwar economic policy, from the time of the Atlantic Charter until the present. Imperial preferences, it is perfectly clear, are to be the British quid pro quo in bargaining about the future level of our tariffs. Such a bargain would be a fair one for us. The conversion of our economy to peacetime purposes will be an extensive process, requiring many adjustments. While we are making radical shifts in population and resources, we might just as well include in the process the long delayed adjustment of American business to a changed tariff environment. Indeed, the reconversion period may be our only opportunity to make a genuine cut in our tariff levels without causing serious disturbances to business.

The financial situation of Britain will be repeated, with modifications, in most of the other countries of Western Europe. The United Nations conference which established the United Nations Relief and Rehabilitation Administration adopted policies which, however wise in the context of the relief problem, will complicate a general restoration of free exchanges. Under the rules of UNRRA, the liberated countries which have gold and foreign exchange resources are to

*Fifth Report of the President to the Congress on Lend-Lease Operations, June 11, 1942, p. 21, Chapter 3.

pay in cash for their relief supplies, and will not receive them through UNRRA. Thus France, Belgium, the Netherlands, and Norway are paying in gold for the civilian supplies they are receiving from the Allied armies, and for the supplies they are procuring independently in the United States, Canada, and other supplying nations. Relief needs, and the cost of preliminary restoration of war damages, will therefore require an immediate drawing down of foreign exchange reserves to levels which the French, Belgian, and Dutch Treasuries will certainly regard as dangerous. They will almost necessarily apply exchange controls which will militate against a quick restoration of freedom of exchange. Each country will face in addition budgetary difficulties, difficulties of internal economic adjustment, and problems of transferring resources which will serve the advocates of autarchy and statism as additional arguments for maintaining and extending wartime controls.

III

The plight of Italy represents another class of cases altogether. The economic situation of Italy is an object lesson in the inadequacy of our policy for dealing with the economic problems of the transition period in countries which have been pillaged and scorched by the Germans, and fought over by the armies. Italy has suffered terrible war damage, and her industrial plant is gravely weakened. She has no reserves of foreign exchange, and practically no current sources of exchange. It will take time before Italian trade can be resumed. Italian production cannot be restored without considerable quantities of imported supplies. For the best possible political reasons, we want to help and support the Italian people and the democratic groups among them which are trying to create a popular and progressive Italian government.

Yet what we are doing is not enough, either in conception or in fact, to meet the needs of the situation. We are importing comparatively large amounts of foodstuffs and other consumer goods into Italy as military relief. By the end of 1944, the civilian supply program in Italy will have cost \$200 million. The principle on which the military relief program is based has been not to pamper the enemy, i.e., to give what is required to prevent food rioting and pestilence along the lines of communications, and no more. These programs do far too little towards restoring production and employment in Italy. They are so weak in agricultural machinery, industrial spare parts, and supplies for utilities and transport that no end is in sight for the present great imports of foodstuffs and consumers' goods. Under the present supply programs it will take years for Italy to become self-supporting and to get off relief. The social and political consequences of such a program of importations are obvious, and unhappy. They cannot provide a foundation for the rebirth of a busy, productive and progressive community life in Italy.

The Italians are supposed to pay for what they receive from the armies. We can hardly give the Italians relief supplies for which we are asking the French, the Belgians, the Dutch, and the Norwegians to pay in dollars. So far it is expected that the Italians will pay for the military relief program with funds credited to them against the local currency required for the pay of our troops in Italy, together with accruals from remittances, exports, and shipping. These devices are not proving sufficient even as a matter of bookkeeping. There are not enough American troops in Italy, nor enough Italian ships earning dollars, to pay for the supplies being brought in. Our supplies are going into Italy as a matter of military necessity. In fact they are going in on a credit

whose terms may not be discussed until a Treaty of Peace is negotiated. Yet we have as yet no alternative way to support the program of Italian reconstruction we want and need, and will have none, unless we change our lend-lease policy, until the Bretton Woods Bank is established, and Italy is allowed to become a member.

Under its original rules, UNRRA funds could not be used in enemy territory. This policy was modified at the recent UNRRA meeting in Montreal, to allow \$50 million to be spent in Italy for three specified purposes--the relief of children, nursing mothers and displaced persons. But this step will do nothing to relieve the crisis in Italy. Fifty millions for children, nursing mothers, and refugees does not begin to measure Italian needs. But even under broader policies UNRRA could not do the job of reconstruction in Italy which needs doing. UNRRA can provide only relief supplies required by victims of war, and such industrial supplies as are needed to facilitate the local production of relief supplies. The scope of UNRRA's supply operations has been narrowly limited as a matter of policy, and UNRRA could in no case do much more than the armies are now doing in Italy. Italy needs industrial supplies which UNRRA is expressly forbidden to provide. Without such supplies there can be no end to the process of relief, no beginning of normal employment, commerce, and growth. In the second place, UNRRA has enough funds in contemplation only to meet the estimated supply needs of China, Greece, Poland, Czechoslovakia, and Yugoslavia, the only countries in which substantial supply operations are planned. It may be expected, therefore, that putting any large part of the burden even of Italian relief on UNRRA will be strongly resisted.

The Italians are asking for lend-lease aid. So far we have hesitated to embark on an ambitious lend-lease program for Italy. Although some lend-lease funds might be used to advantage, during the period of hostilities, lend-lease would not in any sense provide an adequate solution to the Italian problem under its present limitations of policy. Lend-lease is now regarded exclusively as a war supply mechanism. The prevailing legislative and administrative development of policies under the Act would greatly limit the practical usefulness of any recourse to lend-lease in the present situation in Italy or other liberated areas. Lend-lease supplies are, of course, being used in some liberated territories--in the Soviet Union, for example--to facilitate local war production, and other measures of economic mobilization for carrying on the war, and to maintain the civilian economy on a wartime basis. The time has passed, however, when as a practical matter one can say that the larger part of the economic needs of Italy are required in order to win the war.

Nor are private funds available to take up the work of reconstruction. Under the Johnson Act, no Italian governmental loans can be floated here. And Italian credit at this moment would not be very strong. Until the bank planned and projected at the Bretton Woods Conference is established, no American credits for Italy can be expected, beyond the military supply program now in process. And there is a question as to whether the policy of the Bank proposed at Bretton Woods will not prove too orthodox, for the first unproductive work of restoring war damages.

We have thus arrived in Italy at a point of utter bankruptcy of policy. We are sending in a badly planned assortment of minimal civilian relief supplies, without any clear and workable plan for financing their importation or continuing to do so when hostilities cease. We have no policy which would permit us to assist promptly in the reconstruction of Italy, or any other liberated territory,

and there is little or no chance of new legislation being drafted, considered, or approved before the middle of 1945, at the very earliest. Unless we change our present lend-lease policy our only means of financing the export of any supplies after hostilities cease is provided by section 3(c) of the Lend-Lease Act, which contemplates the completion within three years of the undelivered parts of lend-lease programs pending at the termination of other lend-lease powers. This provision will permit a form of surplus disposal on credit terms, but it can be of practical use only in the case of the Soviet Union and Britain, and perhaps one or two other countries with whom we have active lend-lease programs in process. Even in these cases, it will be a clumsy, inadequate, and unsatisfactory approach to any problem but that of surplus disposal.

IV

An emergency policy is urgently needed, if the liberation of Europe, and the tapering-off of present lend-lease war programs, are not to produce economic chaos. The situation of the several countries of Europe will be different, but each will require financial assistance before it will be capable of the kind of liberal economic policy in which we have so great and so selfish a stake. For some time after the war there is bound to be a shortage of dollars on current account. We shall have surpluses to export. No one will be able to buy them. Europe, with its needs for internal reconstruction, will not be equipped to export goods or to provide services on anything like a scale which would permit current payments. Budgets and international accounts knocked into confusion by five years or more of war dislocation will have to be adapted to new circumstances. The continuing flow of needed reconstruction supplies must be assured, on credit terms, during the period of transition, if we want to achieve our essential objectives in the field of international economic policy. The absence of American aid during the early transition period will mean a strengthening of autarchic tendencies. Each country will have to depend on its own resources, on its reparations from Germany, and on its British credits. Under such circumstances, the process of rebuilding will be slow and painful, accompanied by unemployment, and by the uneconomic and subsidized development of some local industries. Such a course on our part would multiply the obstacles in the path of success for the Fund and Bank proposed at Bretton Woods. It would give rise to political disillusion, and greatly strengthen the hands of extremists. The danger of fascism in Europe will not pass with the defeat of Hitler.

Our national interests, strategic, political and economic, would be best served by the recreation of a freer world economy. There is a great danger of our failing to achieve that goal. Time is short, and bold measures must be considered. What can and should be done?

The first step to be taken, beyond the most rapid possible acceptance of the Bretton Woods Fund and Bank, is to inaugurate an entirely new program of Emergency Reconstruction Loan Agreements under the broad authority of the Act to Promote the Defense of the United States, commonly, but misleadingly, called the Lend-Lease Act. These agreements could legally be undertaken without new legislation, although full and advance consultation of the appropriate Committees of the House and Senate would be desirable and normal constitutional practice. An emergency program on these foundations, while hardly an ideal solution, would be as useful an approach to the problem as the state of our statutes will permit.

It would be altogether possible legally to devise an appropriate method under the Lend-Lease Act through which we could join with other United Nations in Financing emergency shipments to liberated areas for the transition period. The Lend-Lease Act was passed before we were at war, and lend-lease funds have been used in South America, the Middle East, and other areas of vital interest for purposes of political stabilization, economic warfare, and other urgent defense purposes. The Lend-Lease Act itself provides for transfers to the government of any country whose defense the President deems vital to the defense of the United States, of defense articles, services and information, when the President deems such transfers to be "in the interest of national defense." It does not require extended argument to prove that vital defense and security interests of the United States would be furthered by the restoration and maintenance in Europe of essential economic activities, on a multi-lateral basis; by the prevention of economic chaos; and by the prompt beginnings of economic reconstruction, during the emergency period before the Bretton Woods plans can go into full effect. We are now sending supplies to the Italian people on what are in fact indefinite credit terms, in order to prevent their misery from interfering with operations. Trade with a restored Italy, and the political cooperation of a democratic Italian government, are no less important to the security and prosperity of the United States, no less directly "in the interest of national defense." The statute is a sufficient legal foundation for a program of emergency reconstruction loans.

Programs of reconstruction should be completely and sharply distinguished from existing lend-lease war programs. They should not be handled under the Lend-Lease Master Agreements, but under new and special loan agreements drafted for the purpose. The ambiguities of lend-lease finance are dangerous, and should be avoided in new situations. The President, the Foreign Affairs and Foreign Relations Committees of the Congress, and various Administration spokesmen have in a long series of statements hammered out a wholly sound line of policy about obligations for war aid under the Lend-Lease Master Agreements. These statements have finally clarified the nature of the lend-lease relationship which has developed with reference to supplies utilized for war purposes. As the unanimous Senate Committee on Foreign Affairs has said: "The security of the United States is benefited under our lend-lease program first and principally by the use of lend-lease supplied in the war which the Axis has undertaken to wage against us. What we sent to our allies for their use in war is part of our own war effort."

"The purpose of weapons, and the materials from which they are made, is to inflict harm upon the enemy. When we send these materials to our allies, as when we send them to our own troops and factories, the benefit we seek and receive is their use against the enemy. This is not a commercial transaction. It is a military move.

"There is no adequate way to value such military moves in dollars, pounds, or rubles. There is no way to compare the price of an American tank with the life of its Russian, British, or Australian crew. Our supplies which go to the war are paid for on the battlefield in the damage they do our enemies."*

*Report to accompany S. 813, 78th Cong., 1st Session, No. 99, Mar. 10, 1943, p.9. See also Report to accompany H.R. 1501, 78th Cong., 1st Session, No. 188, Feb. 26, 1943, pp. 11-13; Whidden, Reaching a Lend-Lease Settlement, Foreign Policy Association Reports, April 15, 1944.

It is thus clear that no one owes us any money for lend-lease supplies used in the course of the war. Unless we want to apply the same rule to lend-lease supplies used for reconstruction, it would simply cause confusion to spend lend-lease funds for such purposes under the present Master Agreements. We should instead make new and distinct agreements to cover the reconstruction programs. Actually a different rule seems appropriate, and should be specified in advance, through favorable but specified interest and repayment provisions. The reconstruction of the European economy is on a net productive activity, and should justify the charge of low interest rates--perhaps slightly above the average carrying charge on our national debt. After all, the famous "War Debt" on which the Finns so conspicuously paid their interest was not a war debt at all--Finland was a Duchy of the Russian Empire during the last war--but a reconstruction loan. The use of lend-lease procurement procedures, which are procedures of United States government procurement, would give us every opportunity to be sure that we were supporting economically justifiable reconstruction programs. We could thus prevent the rebuilding of uneconomic or heavily subsidized industries, and assure ourselves that our loans would earn their interest through their contribution to productivity.

Such a program of Emergency Reconstruction Loans should be accompanied by the repeal of the Johnson Act and a clarification and enlargement of the powers of the Export-Import Bank, or some other appropriate lending agency. The Johnson Act should be interred without comment or trace, and the war debts issue of the First World War decently forgotten. Unless this is done, we are likely to find that the government will emerge with exclusive legal authority to lend money to most of our Allies. Such a development would constitute an unnecessary and undesirable measure of financial monopoly. Private financing, as well as government financing, will be needed in the reconstruction period, and thereafter. The legal barriers to its function should be removed. The government must, of course, have ample power to act in cases which should be outside the scope of lend-lease procedure. Such power should be assured by an enlargement of the authority, and of the lending power, of the Export-Import Bank, which now labors under the legal handicaps of the Johnson Act.

Credits alone may not be sufficient to facilitate the resumption of international economic life on the scale and with the momentum we want to see. The case of Britain represents a class of financial problems which may require still another procedure. The British are reluctant to incur new debts, to add to those which have piled up in the course of the war. The essence of the British problem is different from that of Italy, Greece, Poland, or perhaps France. The British lack gold and available dollars sufficient to act as a monetary reserve during the period of readjustment while their imports and exports reach a new equilibrium with British domestic economic policy and with the changed position of Britain in world trade. If the British had a larger monetary reserve, sterling could be unfrozen immediately at the end of the war, certainly as to current transactions. The transfer of sterling funds into dollars would probably not be great, if stronger reserves fortified confidence in sterling as a currency. It is a common experience in banking that the larger the reserve, the less the danger of a run. And even if the course of events leads to some transfers into dollars, the currency which will most easily command goods in the first post war period, a larger reserve could permit some drawing down of gold holdings without requiring a suspension of free exchange dealings. The reserves could be gradually reconstituted over a period of years, as the British International account finds its new balance.

Two types of remedies suggest themselves. One is the precedent of the Anglo-French financial agreement, which provides in effect for indefinite overdrafts in either direction. For various reasons, this does not seem a practicable approach, unless our Stabilization Fund could be used more imaginatively than it has been used in the past. The second would rest on the example of our lend-lease loans of silver during the war. We have made certain specific loans of silver to meet essential war needs, and to combat inflation, under special contracts calling for the return of the amount of silver loaned, in ounces, at a given period after the war. Comparable loans of a few tons of gold, calling for the return of the same amount of gold after a period of perhaps thirty-five years to fifty years, might put our excessive gold reserves to work with dramatic, even magical effect. With or without changes in our banking regulations, we would have ample excess reserves in gold to undertake such a program without restricting the quantity of money available in the United States. These transactions in gold would in effect be stabilization loans, without interest, and their terms might be broadly adapted to the particular financial circumstances of the countries involved. Stabilization arrangements along these lines may be the cheapest and most practical way to secure an immediate freeing of exchanges after the war, and a consequent beginning of the process of internal and international readjustment to changed economic factors. They might well be handled so as to initiate the trends on the basis of which the Bretton Woods plans could make their maximum contribution to order and progress.

This emergency program for the transition period has four aspects: (1) Reconstruction Loans to finance the flow of American supplies required in the first period after hostilities cease; (2) opening private channels of finance; (3) enlarging the government's power to make other loans that may be needed; and (4) Stabilization Loans of gold as a commodity, to permit the immediate freeing of exchanges. Such a program would give the United States resources with which to secure the basic economic goals of its foreign policy. Reconstruction loans would not burden the American taxpayers, for they should and can be used to finance economically justifiable projects, on which repayment could be expected. Reconstruction is a matter of banking, not of philanthropy, and banking, after all, has always been regarded as a profitable business. Such a program would contribute to the enlargement of employment at home, and to the orderly reconversion of American industry.

Its basic merit, however, is in the field of political and military security. We speak of the coming months and years as a transition period. It is not at all certain, however, that we are going to move in the direction we want. Our goals in the field of international economic policy are perfectly clear, and altogether feasible. But they can be reached only by aggressive action. Without flexible and resourceful economic diplomacy on our part, the likelihood is that the transition ahead will be one towards bilateral trade and restriction, with all the menace they imply to peace and economic welfare. A well-handled flow of American credits are required to make the next period in world economic development one of transition to liberalism, and not to autarchy and reaction. In terms of our national interests, that goal would be worth pursuing even if it cost a good deal of money.