This page follows p. 37.

The strength of the position of those who call for the temporary transfer to an international body of certain sovereign economic powers rests in the conviction that the long-run interests of most countries are best served when no country seeks to gain at the expense of another. It is true that rich and powerful countries can for long periods safely and easily ignore the interests of poorer or weaker neighbors or competitors, but by doing so they will imperil the future and reduce the potentiality of their own level of prosperity. The lesson that must be learned is that prosperous neighbors are the best neighbors; that a higher standard of living in one country begets higher standards in others, and that a high level of trade and business is most easily attained when generously and widely shared.

It is with these thoughts in mind that the following list of conditions for eligibility should be examined.

Any member of the United or Associated Nations is eligible for membership in the Fund provided it agrees:

To abandon, not later than one year after joining the Fund, all restrictions and controls over foreign exchange transactions with member countries, except with the approval of the Fund.

It is important that participating countries be motivated by common objectives in conceiving their foreign exchange policies and desirous of adopting basically harmonious procedures in implementing such policies. Some allowance will, of course, have to be made for reasonable differences because of dissimilarities in the economies of various countries, and early in the Fund's existence there would need to be toleration of lack of uniformity in policy. In general, however, and as basic and long-run prerequisites to participation, it would seem necessary for each member country to subscribe to the general policies of permitting foreign exchange trading in an open, free and legal market, and to abandon, as rapidly as conditions permit, all restrictions or controls by which various classes of foreign exchange transactions have been prohibited or interfered with, other than from consummation in such a free market.

This requirement calls for careful examination. There has been too easy an acceptance of the view that an enlightened trade and monetary policy requires complete abandonment of controls over international economic transactions. There is a tendency to regard foreign exchange controls, or any interference with the free movement of funds and of goods as, ipso facto, bad. This view is unfortunate. It is both unrealistic and unsound. It ignores the fact that there are situations in which many countries frequently find themselves, and which all countries occasionally meet, that make inevitable the adoption of controls of one character or another. There are times when it is in the best economic interests of a country to impose restrictions on movements of capital, and on movements of goods. There are periods in a country's history when failure to impose exchange controls, or import or export controls, have led to serious economic and political disruption.

It probably would be fatal to the Fund, I believe, if the conditions of participation in it were based upon the assumption that no restrictions upon exchange, or upon trade were permissible.

It would be equally unfortunate, however, if it were to be assumed that restrictions on foreign exchange transactions, on the international movement of goods, and the use of multiple currency devices were desirable instruments to employ under all circumstances for safeguarding or controlling international economic relationships. It is easy to exaggerate the need for such instruments and the benefits derived from the use thereof, as it is to exaggerate their adverse effects.

The theoretical bases for the belief still so widely held, that interference with trade and with capital and gold movements, etc., are harmful, are hangovers from a Nineteenth Century economic creed, which held that international economic adjustments, if left alone, would work themselves out toward an "equilibrium" with a minimum of harm to world trade and prosperity.

It is doubtful whether that belief was ever sound. Certainly few competent students of international economic affairs would hold that it applied to present conditions or to conditions likely to prevail during the post-war period.

The forces of adjustment set into motion by changing trade balances, flows of gold or of purchasing power, changes in price levels and all the phenomena that the expert in the subject recognizes as instrumentalities in the so-called mechanism of adjustment of international balances of payment, rarely, if ever, work out quickly enough or effectively enough to be depended upon to achieve good results. In fact, it is doubtful if they ever were depended upon, unaided, to bring about the desired "equilibrium." In modern times, particularly, there has always been somewhere in the picture some measure of control over, some measure of interference with the movement of funds and goods in order to bring about certain desired ends.

The task before us is not to prohibit instruments of control but to develop those measures of control, those policies of administering such control, as will be the most effective in obtaining the objectives of world-wide sustained prosperity. To cast aside certain effective instrumentalities of control because they may be and have been abused, is just as foolish as it would be to rely solely on the self-interest motive of individuals as a means of solving our economic problems.

The requirement suggested above that there be accepted the general policy of foreign exchange trading in open, free and legal markets, and the abandonment as rapidly as conditions permit of restrictions on exchange controls, should be taken to mean that there shall be acceptance of the principle that controls and restrictions will be employed only when they are clearly justified by the economic circumstances, and only to the extent necessary to carry out a purpose contributing to general prosperity. The chief difficulty in the application of the principle will be agreement as to what is in the interests of general prosperity. The danger of conflicting policies lies not only in the difficulty of distinguishing between real and specious advantage, i.e. between the advantages of a special group as against the advantages of the whole--but much more in the difficulty of reconciling short-run interests with long-run interests. One of the purposes of this fund is to provide for a more reasonable basis for such distinction, and to supply the means through which it will be possible to pursue long-run and broader interests, without too great a sacrifice of the narrower and short-run interests.

The second requirement or condition for participation should be the acceptance of the principle that no participating country will alter its exchange rate on currencies of other countries without the consent of the Fund.

This condition is very important. Its obvious purpose is to eliminate the possibility of competitive depreciation of currencies. It recognizes that there are occasions when it may be economically wise for a country to increase or decrease the value of its currency in terms of other currencies. When a country's balance of payments is in disequilibrium for causes that do not appear to be temporary, and if that disequilibrium uncorrected will deplete a country's foreign exchange reserve, then altering the value of that currency in terms of other currencies is one of the ways in which the disequilibrium could be corrected. Other ways of correcting disequilibrium in the balance of payments are the imposition of restrictions on imports and subsidy of exports, either directly through import and export controls, or through use of exchange controls or multiple currencies. Which method or methods are best suited to accomplish the objective depends on the cause of the disequilibrium, the circumstances, the country, and the time. The circumstances under which it may be wise to alter an exchange rate in order to correct maladjustments of the balance of payments have long been a matter of controversy among monetary theorists. But there is general agreement that an alteration in the value of a currency in terms of gold (or in terms of important currencies) is a very serious business and one not to be undertaken lightly. The change in the value of a currency in terms of gold or of other currencies means that a change has been imposed by that act on the other currencies. When, for example, the dollar changes in terms of sterling, obviously sterling changes in terms of the dollar. Because all countries are to a lesser or greater degree affected by the action of any one country with respect to the value of its currency, it is only reasonable to demand that such action should not be undertaken without some careful weighing of the consequences of the action on other countries.

The purpose of requiring approval by the Fund as a condition of alteration of currency is to assure joint consideration of the merits of the proposed action and thereby avoid unilateral action taken to obtain presumed competitive short-run advantages irrespective of the consequences of the impact of the step on other countries or even on the same country. The mere fact that membership would be forfeited if a country acted contrary to the wishes of the majority in so important a matter would make countries hesitate to undertake lightly a change in their currency. The very discussion of the problem by competent representatives of various countries will in itself be a potent influence to avoid unnecessary changes. It will, moreover, be an assurance that when a change is made it will not be a signal for numerous other countries to follow in their own real or presumed interest.

There will be difficulties surrounding the operation of this condition, the most important of which would be the necessity for secrecy when a country is contemplating a step such as altering the value of its currency in terms of other currencies. If a country believes that it should depreciate its currency relative to others, it could hardly throw that matter open for public discussion. By so doing it would stimulate speculative activities in the exchange market which might have the effect of precipitating the very action being considered. Some procedure would have to be devised to make possible deliberations without publicity. It might be that an Executive Committee could undertake to pass on such cases, or it might be possible to arrange that during such discussions no country will accept or permit movements of capital to and from a country considering the step.

Some objection to this requirement will doubtless be raised on the ground that such a provision means that other countries pass judgment on what is a domestic monetary matter. The necessity for obtaining approval of other countries on such a matter will be regarded in some quarters as a serious infringement of sovereignty. There is some measure of truth in this but hardly enough to constitute a decisive reason for not participating in the Fund. Alteration of a currency affects other countries as well as the country making the change. It is, therefore, only reasonable to demand that the other countries have some say in the decision. Furthermore all members would be surrendering their "rights" to an equal extent. Unless nations are willing to sacrifice some of their power to take unilateral action in matters of international economic relations, there is very little hope of any significant international cooperation--let alone collaboration. To avoid giving richer nations greater authority on such matters, by virtue of their larger number of votes, it may be desirable to give each participant only one vote when questions of altering currency rates are being voted upon. As a last resort, a country always has the choice of withdrawing from the Fund so that it can always preserve its sovereignty in monetary matters if it feels it is being prevented by the Fund from taking action deemed important to its own interest.

The principle worked only tolerably well in the Tripartite Accord during 1935, 1936 and 1937, but better machinery for more adequate discussion and greater willingness to recognize the legitimate interests of other countries, needs to be developed to achieve best results. In evaluating the need for collaboration on questions of foreign exchange rates, it is well to remember that unilateral action can easily be neutralized by similar action on the part of other countries. When a competitive advantage is sought it is essential if it is to be successful that other countries do not take similar action. Otherwise the advantage hoped for is lost. Where the chief objective sought is not a competitive trade advantage in the international market but modification of the domestic price structure or money market, the favorable effects cannot be wholly negated by action of other countries. Since, however, the chief reason for establishing the requirement is to avoid competitive depreciation of currencies, the fact that unilateral action can be easily neutralized constitutes an important argument for securing approval of the Fund before taking such action.

Each country agrees (a) not to accept or permit deposits or investments from any member country except with the permission of that country, and (b) to make available to the government of any member country at its request all property in form of deposits, investments, securities, safety deposit vault contents, of the nationals of member countries, under such terms and conditions as will not impose an unreasonable burden on the country of whom the request is made.

This is a far-reaching and important requirement. Its acceptance would go a very long way toward solving one of the very troublesome problems in international economic relations, and would remove one of the most potent disturbing factors of monetary stability. Flights of capital, motivated either by prospect of speculative exchange at one time or another, exercises control over the inflow and outflow of investments, but without the cooperation of other countries such control is difficult, expensive, and subject to considerable evasion.

It would seem to be an important step in the direction of world stability if a member government could obtain the full cooperation of other member governments in the control of capital flows. For example, after the war a number of countries could request the United States not to permit increases in the deposits or holdings of their nationals, or to do so only with a license granted by the government making the request. Or, some countries greatly in need of capital might request the United States to supplement their efforts to attract capital back to the native country by providing information, or imposing special regulations or even special taxes, on certain types of holdings of the nationals of the foreign countries.

The search for speculative exchange gains or desire to evade the impact of new taxes or burdens of social legislation have been one of the chief causes of foreign exchange disturbances. Less hectic and less dramatic yet in the case of some countries during some periods capable in the long run of even greater harm is the steady drain of capital from a country that needs the capital but is unable for one reason or another to offer sufficient monetary return to keep its capital at home. The assumption that capital serves a country best by flowing to countries which offer most attractive terms is valid only under circumstances that are not always present.

A good case could be made for the thesis that a government should have the power to control the influx and exflux of capital, just as it has the authority to control the inflow and outflow of goods and gold. In fact, virtually every participating government has already practiced these controls to some extent during this war. The consequence of cooperation in this matter among the member governments would give each government much greater measure of control in carrying out its monetary and tax policies. Such an increase in the effectiveness of control means, however, less freedom for owners of liquid capital. It would constitute another restriction on the property rights of the 5 or 10 percent of persons in foreign countries who have enough wealth or income to keep or invest some of it abroad, but a restriction that presumably would be exercised in the interests of the people--at least so far as the government is competent to judge that interest.

The inclusion of this provision does not mean that capital flows between foreign countries would disappear or even greatly subside; it means only that they would not be permitted to operate against what the government deemed to be the interests of any country.

<u>A fourth condition might be that each country agrees not to enter upon any bilateral clearing arrangements except with non-member countries, and then only with the consent of the Fund, and to establish no geographically preferential exchange rates.</u>

The justification for setting up this requirement for participation is to eliminate discriminatory practices in foreign trade which result in friction, unfair competition, retaliation, and sharp trade policies which serve to disrupt good economic and political relations. It means that for the sake of the larger good to be obtained countries agree to give up opportunities for making certain advantageous arrangements. If each country is to operate in accordance with its own immediate interest, irrespective of long-run effects and irrespective of the impact of its actions on other countries, a repetition of the pre-war chaotic conditions in trade will result and again threaten political and economic stability of other nations. The task which confronts the high officials of all nations is to make possible a high level of business activity and of foreign trade within the framework of reasonable and fair foreign trade practices. Just as individuals subscribe to a government of law to obtain maximum prosperity and effectiveness for the whole group, even though adherence to that law involves restrictions on individual behavior at numerous points, so must nations give up lesser advantages for greater good. The concept of sacrificing some immediate benefits for the sake of larger good is the foundation stone of peace and economic collaboration among nations, just as it is the keystone of peace and prosperity within a nation.

The operations of the two agencies discussed in this report should help considerably to remove the justification for trade practices adopted to protect or strengthen an exchange position.

There are times when gains could accrue from bilateral clearing arrangements without significant adverse effects on other countries, but in general the operation of the

Fund should have the effect of making such clearing arrangements much less profitable as among members of the Fund. One of the specific objectives of the Fund is to make available for each member a supply of foreign exchange adequate to enable it to operate more freely and with a higher level of trade than would otherwise be the case. Nevertheless, in the interest of flexibility, and to take care of those situations in which circumstances may warrant a bilateral clearing arrangement, it should be possible for a country to enter upon such an arrangement provided it can obtain the Fund's approval. Discussion by the Fund of such proposals do not require the secrecy or the speed involved in consideration of alterations of exchange rate, and discussions of the advantages and disadvantages of the particular proposal should prove beneficial. An objective decision on the economic wisdom of such proposal is more likely to emerge from the discussion by the appropriate committee of the Fund than from the consideration by one or two countries alone where vested or political interests are likely to dominate the decision.

A fifth requisite for membership might be subscription to the principle that no monetary or banking or price measure or policy would be adopted, the effect of which, in the opinion of a majority of the member votes, would be to bring about sooner or later a serious disequilibrium in the balance of payments, if four-fifths of the member votes of the Fund submitted to the country in question their disapproval of the adoption of the measure.

This provision would prove to be more troublesome than any of the others and yet it would seem to be important to the successful functioning of the Stabilization Fund. Serious inflation or deflation in any one country would affect not only exchange rates and trade, but price levels in other countries as well. It is impossible for any country to take action of that character which does not have important effects on other countries with whom it competes or with whom it carries on trade. The decision as to whether a particular measure or policy contemplated would bring about a serious disequilibrium in the balance of payments would be a difficult one on which to get agreement. To estimate even very roughly the quantitative effects of any given measure on a country's balance of payments is a very difficult task at best. After sufficient agreement was reached on that point it would be even more difficult in many cases to get any measure of agreement as to whether the adoption of the measure in question was economically wise or not.

There are times when domestic consequences are sought which are more important to a country than the adverse effects that might follow in some directions from the accompanying disequilibrium in the balance of payments. There are other instances in which disequilibrium provides a necessary corrective, and frequently a country is confronted with only poor choices and disequilibrium is the least undesirable of them.

To assume that it would ever prove easy to get four-fifths of the member votes to take so drastic step as to disapprove a measure proposed by a sovereign government deemed by it to be in its own interest, is to ignore the known complexities of the monetary problems, and the political realities of international relationships.

Notwithstanding the difficulties involved in exercise of a veto power by the Fund of monetary measures, there will be instances in which the case is clear enough and the consequences important enough to justify the exercise of that power. It is assumed that the Fund would not concern itself with minor measures. To help avoid the error of attempting to evaluate measures which are not important, the requirement provides that a majority of the members would have to be of the opinion that the results of any given measure are likely to be serious. It then requires four-fifths of the member votes to authorize official disapproval. It may well be that despite this degree of protection against arbitrary action or needless interference most countries would object to subjecting what they believe to be purely domestic affairs to international supervision. If compromise with this view is found feasible, it is hoped that it takes the form of requiring a larger majority-- say 90 percent instead of 80 percent of the member votes, or, as a last resort, requiring that the disapproval of the Fund call forth the promise of the offending country to reexamine her position in the light of the Fund's report.

In any case, the discussion which would take place by an international committee of the character envisaged--men expert in their fields, international in their outlook, and scientific in their approach--could not help but prove very salutary. The educational process to which officials, administrative and legislative, in each country would be subjected in defending specific policies or measures before such a committee would in itself go a long way toward improving the quality of monetary, credit and banking policy. It probably would be necessary for the committee, certainly during the early years, to be very tolerant of policies pursued by participating countries. Gradually, however, there should develop a greater reluctance on the part of member countries to take measures which do not meet the approval of the majority of the members of the Fund. The success of the Fund in this field would depend in large measure upon the wisdom with which matters of this kind are examined and the degree of sympathetic understanding they are capable of displaying

The member countries agree (a) to embark within a year after joining upon a program of gradual reduction of existing trade barriers--import duties, import quotas, administrative devices--and (b) further agree not to adopt any increase in tariff schedules, or other devices having as their purposes higher obstacles to imports, without giving reasonable opportunity for the Fund to study the effects of the contemplated change on exchange rates and to register its opinion. In rendering an opinion the Fund will make recommendations to which member governments agree to give serious consideration.

It might contribute notably to conditions tending to promote exchange stability if participating countries, particularly those with large reserves of foreign exchange, were to agree to a gradual reduction of duties on imports. It might be possible to devise an acceptable formula for general and gradual tariff reduction to a level more in harmony than were tariff policies of the twentieth century with the objectives of reducing the causes for international friction and increasing the standard of living the world over. Those high tariff policies in the main reflect adherence to the traditional, crude, mercantilist fallacies. So widely held are those fallacies, so persistently clung to by persons who should know better, so potent are they in shaping many aspects of domestic and foreign policy, and so unfortunate in their effects on world peace and prosperity, that one is tempted to list "mercantilism" or its more expressive heir "protectionism" as "World Enemy No. 1."

Yet, though there is no doubt as to the evils of crude protectionist policies, caution must be exercised in attempting to translate a policy of lower tariff schedules into an actual program. There is danger of retarding progress by advocating a trade policy which ignores the sound basis for the existence of some import duties. There is too easy an assumption that as much reduction as possible in all duties is desirable; that any movement toward free trade is, ipso facto, a good thing for the world.

In their reaction against the crude protectionist fallacies that a country with high standards of living must adhere to a policy of high tariff schedules if it is to prevent widespread unemployment or deterioration of its high standard of living, they are inclined to throw the baby out with the bath and assume that all duties are bad; that free trade, or rather tariff for revenue only, is the ideal toward which all enlightened nations should move as rapidly as possible.

The belief that reduction in all import duties increases trade and yields a higher standard of living for all countries under all circumstances and in all stages of their economic evolution assumes that countries are usually utilizing virtually all their capital and labor; that a country chiefly agricultural in its economy has as many economic, political and social advantages as a country whose economy is chiefly industrial, or a country which has a balanced economy; that there are no gains to be achieved by great diversification of output. These assumptions, essential to the belief that "Free Trade" policy is ideal, are not valid. They are unreal and unsound. "Free Trade" policy grossly underestimates the extent to which a country can virtually lift itself by its bootstraps in one generation from a lower to a higher standard of living, from a backward agricultural to an advanced industrialized country provided always it is willing to pay the price. The view further overlooks the very important fact that political relationships among countries being what they are, vital considerations exist in the shaping of the economic structure of a country other than that of producing goods with the least labor.

The subject of the best tariff policy for a given country at a given period in its history is a most interesting one, but justice could not be done to it in the space that could reasonably be allocated to it here. A great deal has been written on the subject and the interested reader in his search for sound policy will find that the complexity of the problem is apt to increase with the profundity of his reading. Yet one conclusion is certain to emerge from his study of the subject, namely, that most import duties are too high, that many duties remain too long, that few are imposed for sound reasons, and virtually none of them are re-evaluated often enough by the law-making bodies in the light of changing needs and conditions.

The value of requiring participating governments to agree to a general policy of lower tariffs lies solely in the recognition that most duties in the tariff schedules of every country, at their present level, are inexcusable on any economic, political or social grounds. Their existence merely reflects uncritical adhesion to protectionist policies or the successful pressure of some powerful vested interest, or both. It is to place on the ~~defense~~ we obstructions to trade, whether in the form of unreasonably high duties or in any other form that subscription to a commitment of lower tariff policies might be justified.

Yet, it cannot be overlooked that the shaping of tariff policy has been for too long the prerogative of lawmaking bodies, and the battleground of legislative maneuvering to expect the Congresses and Parliaments to subordinate their authority on such matters to an international body. If the sugar, wool, wheat growers of the United States, and the shoe and textile, pottery, and steel manufacturers--to name only a few of the industries insisting on high protective duties--were to see in any suggested agency a definite threat to what they regard as necessary protection to their industry, they would combine and probably rally enough support to their crusade to ruin the prospects of acceptance by Congress of any proposal no matter how attractive the scheme may be to economists, statesmen, foreign trade associations, college professors and bankers.

It would seem to be a far wiser policy not to attempt too much and thereby jeopardize any but an innocuous program.

On this issue, as on no other, prudence dictates compromise. The most one can hope to get is adherence to a principle without surrender of any authority. Hence the requirement calls only for public adherence to the stated principle, and permission to the Fund to submit a report giving reasons for its disapproval of an added barrier to trade if the Fund deems it harmful. If any international agency or organization wrings more than that out of the American and other publics, a miracle in economic morality will have been wrought by this war.

Another possible condition of participation that merits attention is the agreement that no Government or Central Bank shall default on its external obligations, or any part thereof, without consent of the Fund.

This requirement has considerable possibilities for good. If the flow of private capital from capital-rich to capital-poor countries is to be stimulated and the flow of specialized capital among countries is to be fostered, something drastic must be done to reestablish confidence of private investors in the integrity of foreign borrowers. Defaults by governments and states have been in the past too easy a way out of foreign exchange and budgetary difficulties. The defaulting country frequently experiences an immediate gain but unfortunately the long-run losses have far more than outweighed the gains. If the Fund and the Bank could be a potent force for preventing defaults (as well as keeping interest rates reasonably low), a long step forward will have been made toward the increased productiveness of all countries.

It can hardly be expected that objective decisions on defaults can be made by the defaulting country or by the country gaining most by continued servicing of a debt. To make what takes on the character of compulsory arbitration in debt adjustment an acceptable and workable instrument, the proposed judgment must be that of a large group of nations, the majority of whom are not directly and immediately affected by the decision. Consideration of the pros and cons of a contemplated default by the Fund would seem to promise that kind of objectivity, and therefore not be a requirement that would stand in the way of acceptance by any government.

Not to subsidize--directly or indirectly--the exportation of any commodity or service to member countries without consent of the Fund.

One of the unfair trade practices frequently resorted to in the past has been export subsidies. Most countries have been guilty of subsidizing some exports either by direct or indirect methods. It is easy for the practice to grow as there are in every country powerful interests who because of a monopoly position or political influence, at the expense of the public, are able to keep up the price of a product at home by practicing subsidized dumping on foreign markets. This device in essence is no different from the use of multiple currencies or special clearing arrangements except that the gain in the latter case is shared by more persons. They all aim to undersell a foreign competitor not by offering the same goods at a lower price, or better goods at the same price, but by undercutting a foreign competitor at the expense of the taxpayer of the exporting country.

It is just such practices that give rise to rivalries which constitute fertile soil for international friction. If subsidies to exports are condoned there is no logical justification for objecting to any kind of trade device designed to increase exports or decrease imports. The result would be a repetition of the ruthless fight for foreign markets that characterized international trade in the 'thirties.

It might be possible to obtain acquiescence among the member countries not to resort to the more obvious forms of subsidies without consent of the Fund. Since the Fund would be a sort of court of appeal, the possibility of subsidizing the export of a commodity or service exists. Yet presumably it would be invoked only under special circumstances. The fact that approval of the Fund were necessary would be helpful to governments in their struggle against vested groups seeking special advantages. Though it will be found very difficult to get a satisfactory working definition of an indirect subsidy, it should be at least possible to define the term so as to apply to the more obvious devices.

The Fund would probably have to permit subsidies to shipping and air travel. Almost every country subsidizes these two for military reasons, for economic reasons, and reasons of national prestige. It is irrelevant that much of the defense for shipbuilding and shipping based on economic and patriotic grounds is specious. These subsidies are so deeply imbedded in custom and policy that it is useless to attempt to modify them through an agency such as we are discussing.

Subsidies to tourists, to student voyages, etc., are of a different character. It may well be in the interests of all countries, and certainly is in the interests of some countries, to attract tourists by subsidies of one form or another. This subsidizing of exports of services seems to arouse little objection in the importing country (i.e. in the countries whose nationals do the touring) and can at least be defended on social and cultural grounds. Since United States is probably the most generous producer of profitable tourists, there is an added justification for attracting Americans abroad by subsidies if necessary, namely it will help the United States to develop a much desired "unfavorable" balance of payments through the most desirable available channels.

All considered it were probably better to exclude "services" altogether from the prohibition of subsidies, and save the Fund much trouble. It would, moreover, make it less unlikely that the requirement would find acceptance by enough nations.

It may be properly questioned whether an agency of this character is the appropriate instrument for obtaining fair trade practices in foreign trade. It might be that some other agency like a league of nations should be the vehicle, or possibly dependence should be on a program of multilateral treaties. However, it does seem that it should be less difficult to obtain agreement on such matters when the vehicle is an agency, membership in which has obvious economic advantages. Moreover, a country could feel it could always withdraw from the Fund if it deems its interests significantly harmed by failure to obtain approval of the Fund for a contemplated action.

Restrictions on membership

No restrictions as to membership should be imposed on grounds of the particular economic structure adopted by any country.

There are certain to be some persons or governments, who either out of fear, or prejudice, or dislike would wish to exclude Russia from participation in an international undertaking of the character described in the previous pages. Yet to exclude Russia would be an egregious error. Russia, despite her socialist economy could both contribute and profit by participation. To deny her the privileges of joining in this cooperative effort to improve world economic relations would be to repeat the tragic errors of the last generation, and introduce a very discordant note in the new era millions everywhere are hoping for. If the Russian Government is willing to participate, her counsel in the preliminary negotiations should be as eagerly sought as that of any other country, and her membership in both Fund and Bank equally as welcome.

A socialist economy like a capitalistic economy engages in international trade and financial transactions which can be either beneficial or harmful to other countries. In fact, because the conduct of foreign trade and international financial transactions are exclusively the creature of the government in a socialist economy, there is all the more reason to attempt to get them to join in a cooperative attempt to introduce stability in international economic relationships and a higher level of trade. If for no other reason than that there are no limits to which a powerful socialist economy could go if it sought to disrupt trade. It would be extremely shortsighted not to welcome Russia to participate.

IV. Composition of the Fund

The Fund shall consist of gold, member country currencies, and member government securities, in such amounts as shall be indicated by a formula set forth in the Agreements. The total subscription to the Fund shall be the equivalent of at least $5 billion.

The task which the Fund would be expected to perform would involve transactions of large magnitude; it therefore should have large resources available. Moreover, the greater its resources the more potent could the Fund be in preventing monetary disruption and in reducing the frequency and duration of periods of disequilibrium. Considering the likelihood that the number of participating governments might be at least a score, a total subscription of the equivalent of several billion dollars would seem to be both possible and desirable.

To avoid tying up funds that would not be needed for some time, if ever, the participants could be required to subscribe only 25 percent of their participation in cash. An additional 25 percent could be subscribed in obligations of the participating government. These obligations would yield revenue to the Fund, and would also supply a source of additional funds to be tapped if and when needed. They would also provide the Fund with the means of conducting open-market operations in any given country when desired. To reduce the cost to participating countries, it might be found preferable to make the securities a renewable three to five-year note, rather than a long-term bond, thus reducing the interest rate and increasing their marketability.

The remaining 50 percent of the subscription should be paid in such installments and in such form as shall be determined from time to time by the Fund.

The Fund would need local currencies and gold to carry on its operations. The provision that half the initial payment of 25 percent be in gold and half in local currencies takes care of that, and also makes participation easier for those countries having little gold. For a few of the countries--e.g. the United States--gold and local currencies are synonomous for purposes of international transactions. One of the objectives of the Fund is to increase the number of countries about which that could be said.

In view of the fact that the gains from participation in the Fund would not take the form of a distribution of substantial profits, the sum each member country should subscribe can hardly be left to the decision of each country. It is hoped that the Fund would show an annual profit but the purpose of the Fund is not to make profits but to help achieve much more important objectives that are not susceptible of measurement in terms of money profits. The Fund would be a cooperative enterprise operated for the benefit of all the participating nations, and each participant should subscribe at least its reasonable share of the total capital necessary, though it could subscribe more if it wished to do so. The share of the total each country subscribes should be determined by some agreed upon formula which would give due weight to various pertinent considerations.

There follows an illustrative formula that attempts to measure the minimum amount of funds each participant should be required to subscribe. The items listed are those which seem most pertinent, and the weights ascribed to each attempt roughly to reflect the importance of that item to the benefits that might be expected to result from participation and the ability to contribute to the Fund's capital.

1.	Gold holdings..........	100	points	for	every	billion	dollars
2.	Gold production........	50	"	"	"	"	"
3.	National income........	2	"	"	"	"	"
4.	Foreign trade..........	25	"	"	"	"	"
5.	Population.............	10	"	"	"	hundred	million
6.	Foreign investments....	25	"	"	"	billion	dollars
7.	Foreign debts..........	10	"	"	"	"	"

Applying the above weights to the situation in some selected countries, the following approximate scores would result:

United States	1,200	U.S.S.R.	400
United Kingdom	300	China	200
Canada	100	Mexico	25
Netherlands	200	Brazil	25
Norway	30	Colombia	20

Converted into dollars, the contributions would be something like the following:

TABLE

(In millions of U. S. dollars)

(Though the contributions or investments would be in the form of gold or local currency, they are converted, for convenience, into U. S. dollar units in the table below)

United States	2,000	Argentina...........	50
England.............	500	Mexico..............	50
U.S.S.R.	400	Brazil..............	50
Canada	50	Colombia	25
Netherlands	100	Cuba	25

The purpose of the table is merely to suggest a pattern of quotas for discussion, and not to lay down any precise pattern or formula. An attempt was made to present a pattern of quotas, the general character of which probably could be defended on logical grounds, but it is certain that a more appropriate formula could be worked out if several minds focused on the problem.

If only 50 percent of the participation were called for, and only half of that in cash, the amounts indicated in the above tables would not be onerous. The United States would be called upon to subscribe $500 million in cash and Cuba only $12-1/2 million. That would be the minimum. They could, of course, subscribe more if they wished. Experience would show whether the total was much more than was needed, or much less. If more were needed the securities could be converted into cash and the remaining half called in. On the other hand, if after long experience it is found that even the initial payments were greatly in excess of needs, it would be an easy matter to return the excess. Since the Fund should be ample to take care of periods of special stress, many years would have to pass, however, before enough experience is acquired to determine the most appropriate size of the Fund. It would certainly be better in the beginning to err on the side of having too much rather than not enough. The effective strength of the Fund and its ability to instill confidence in the currency stability of its participants will be enhanced with the ease with which the Fund can be expected to meet all legitimate claims on its resources. A sum of several billions of dollars does not, therefore, seem inappropriate to the task.

Inasmuch as some of the assistance the Fund can give to member countries is directly proportional to the sum of participation of that country, there will be a strong incentive for some countries to make their participation larger than the scheduled amount.

The Bank for Reconstruction and Development of the United and Associated Nations could be called upon to participate to the extent of possibly $100 million.

V. Management

Where control of the Fund shall be vested is a matter of paramount importance in the formulation of a workable plan. The magnitude of the Fund, the broad scope of its likely powers, the requirements for continued eligibility of participants, together make the question of situs of control important.

The management of the Fund should be vested in a Board of Directors consisting of the representatives appointed by the member governments, each government to appoint one representative.

It would be easy to reach agreement that the most convenient and simplest device would be to vest control of the Fund in a board of directors, to consist of representatives appointed by member governments, each government appointing one representative. It probably would be desirable to have each government appoint an alternate as well. In view of the technical nature of many of the problems, the governments might wish to select as alternates men who would be more qualified than are likely to be the representatives to take up the kind of problems that would most frequently come before the Fund. The representatives would probably be selected from more responsible posts than the alternates, and would likely be concerned with the larger and less technical issues involved in decisions.

The Board shall elect a chairman and a small operating committee.

With a body so unwieldy as it would likely be with representatives from each government, added to the fact that many of such representatives could devote only brief periods away from their home governments, it is virtually essential that the day-to day-operations of the Fund be handled by a small operating committee of representatives. Such a committee would be able to devote full time to the task of managing the Fund, and would, of course, have to be adequately compensated. The election of this operating committee by the member participants would insure the selection of a competent group and the brief period of their tenure of office before reelection would assure also a responsiveness to the wishes of the board. Delegation of authority by the whole board to the committee on many matters could be safely made, leaving larger policy decisions to be referred to the entire board. It is to be expected that the operating committee would have the assistance of a competent technical staff.

If a Fund were to be established with anything like the powers and resources outlined in this report, it would need the services of a large staff of the best experts available. Nothing would injure the changes of effective and successful operation and of making a major contribution to the solution of some of our most troublesome international economic problems than mediocrity in directors and technical staff. A board the size of the one recommended here can, of course, assimilate without serious damage some stuffed shirts, some narrow-minded nationalists, and a few bankers with counting house ideals. But the board will have to include more than a sprinkling of economic statesmen, forward looking, of broad vision, comprehensive experience, world outlook and tenacity of social purpose. The technical staff will have to be headed up by experienced analysts with a thorough knowledge of monetary theory and international economics, with intellectual integrity and aggressiveness, and also include a generous ~~sprinkling~~ quota of eager, able, young men who have been at or near the top in their scholastic achievements and technical writings. The United and Associated Nations can produce plenty of such men.

In all voting by the board, each representative should have one hundred votes, plus one vote for every million dollars of gold (computed at $35 an ounce) turned over to the Fund, plus one vote for the equivalent of every $2 million of local currency originally turned over to the Fund.

There would be little difficulty in reaching agreement that some such set-up as the board working through a committee as outlined above would provide a satisfactory working arrangement, but the real problem is how to distribute the voting power. If each member of the board were to be given an equal vote, then a small country that invested one million dollars would have as much power in making decisions as a country that has subscribed a hundred or a thousand times that amount. With the possibility that the number of small countries participating will be much greater than the large countries, a one-vote-one-member arrangement is palpably unwise. On the other hand, to accord voting power strictly proportionate to the value of the subscription would give the one or two powers control over the Fund. To do that would destroy the truly international character of the Fund, and seriously jeopardize its success. Indeed, it is very doubtful if many countries would be willing to participate in an international organization with wide powers if one or two countries were to be able to control its policies.

It is clear that the voting power must be so arranged as to steer between these two evils. This might be accomplished by working out some compromise between the two bases of voting power referred to above. By giving each member 100 votes plus one vote for every million dollars of gold invested in the Fund, plus one vote for every $2 million of local currency, a satisfactory distribution of control might be approximated. Thus, if the United States subscribes $1 billion--half in gold--it would have 100 plus 500 plus 250 votes, or a total of 850 votes, whereas a country contributing $10 million, half in gold, would have 100 plus 5 plus 1 votes, or a total of 106. With such an arrangement ten small countries could outvote the United States. If any country felt the arrangement agreed upon did not give it an adequate share of control, it could increase its contribution.

A country should have the privilege of replacing, wholly or in part, its securities, or currency with gold. The number of votes its representatives can cast would alter accordingly.

This provision would supply some flexibility in the assets a country turns over to the Fund, and also provides a means whereby a country could increase its voting power. How important the provision might prove to be is uncertain, but in the beginning at least it would appear desirable to introduce flexibility wherever possible.

<u>All decisions, except where specifically provided otherwise, should be decided by a simple majority of the votes cast.</u>

To give adequate protection to each country, most of the important decisions could be made to require more than a simple majority of the votes.

<u>The President of the Bank should be a member of the Board, and would have 100 votes.</u>

Because of the interdependence of the two institutions--the Fund and the Bank--close liaison and opportunities to harmonize policies would be helpful. Both agencies would have broad objectives, both would be international in their outlook, and both would be motivated by the desire to promote worldwide peace, prosperity, and stability. Each would be undertaking responsibilities that call for analyses and judgments of economic situations and trends. The operations of each would affect the other, and the decisions of each should be partly based on the knowledge, plan and judgment of the other. There, therefore, is much to be gained by close liaison between them. That is why the head of each should be a director of the other.

To avoid cumulating voting power, however, the Bank should not be able to cast votes in excess of the minimum, irrespective of the extent of its monetary participation.

PART III

Bank for Reconstruction of the United Nations and Associates

I. Purpose

The objectives of the Bank are: To provide capital for the economic reconstruction of the United Nations; facilitate a rapid and smooth transition from a war-time economy to a peace-time economy in the United Nations; supply short-term capital for the financing of trade among the United Nations--where such capital is not available at reasonable rates from private sources; and help strengthen the monetary and credit structures of the United and Associated Nations by redistributing the world gold supply.

To eliminate the danger of world-wide crises that are financial in origin, and reduce the likelihood, intensity and duration of world-wide economic depressions; raise the productivity and hence the standard of living of the peoples of the United Nations.

To promote a greater degree of economic cooperation and collaboration among the United Nations; make easier the solution of many of the economic and political problems that will confront the "peace conference".

To enhance the opportunity throughout the world for a healthy development of democratic institutions; help assure a distribution at fair prices of important scarce raw materials; and promote stability in prices of important commodities.

Finally, the Bank would provide for the financing and distribution of foodstuffs, clothing and other essential commodities that will be needed in large quantities for the relief of populations devastated by war conditions.

A perusal of the outlined objectives will reveal that they constitute quite an ambitious list. They include some mighty important purposes. Yet, given the resources and powers suggested below, and managed in a spirit appropriate to the importance of the task, there is every reason to expect that substantial progress can be made toward each of the goals listed.

The objectives of the Bank, it will be noted, are similar in some respects to those of the Fund, but a careful examination will reveal that in their most important aspects they are different. The Fund is designed chiefly to prevent the disruption of foreign exchange and to strengthen monetary and credit systems and help in the restoration of foreign trade, whereas the Bank is designed chiefly to supply the huge volume of capital to the United Nations and Associated Nations that will be needed for reconstruction, for relief, and for economic recovery.

The end of the war will find us confronted with an unprecedented demand for capital. The actual physical destruction caused by the war in Europe, Asia and Africa will be stupendous. Factories and public works will have to be rebuilt; hundreds of thousands of homes and farms will have to be rehabilitated; public utilities, transportation systems, which have been destroyed or deteriorated, will have to be reconstructed and improved. Millions of farmers will need to be supplied with seed, fertilizer, livestock and new equipment. Monetary and banking reserves will be depleted. Finally, most of the industry in Europe now geared to supply war demands will need to be transformed to produce peace-time goods. All this will require billions of dollars. If a substantial portion of the capital needed for this tremendous task of reconstruction can be supplied, we can help prevent social disintegration and political disturbances in the defeated countries, and also have an excellent chance of preventing the development of a post-war depression.

To supply this capital at rates of interest low enough and period of repayment long enough to give the borrowing country reasonable hope of being able to repay the loan, is the prime task and justification for a Bank of the character envisaged in this report.

It must be recognized that private capital will not perform this function. It has suffered too many losses. It has been too severely discouraged by depreciating currencies, exchange controls and defaulting governments, to justify the hope that investors will lend large sums to a foreign country, except possibly at rates of interest which would make such loans extremely dangerous because of the burden they would put upon the borrowing country. Only a non-profit institution with enormous resources can afford to undertake the task of supplying adequate amounts of capital on the gigantic scale that will be necessary after the war. Only an international governmental organization can make such loans under the kind of conditions which would help promote and sustain prosperity rather than sow the seeds for future trouble.

Once the combined operations of the Fund and the Bank serve to restore confidence in the continued stability of exchanges, and freedom from restrictions on withdrawal of profits, private capital will probably flow in large volume to areas badly in need of capital. At the beginning these foreign investments will take more ~~lik~~ely the form of branch plants, complete ownership of mines, factories and plantations. With the restoration of confidence they will take on more and more the form of loans to governments, to municipalities and finally to foreign corporations. It is to free the tremendous accumulations--past and future--of private capital to seek profitable employment in countries that sadly lack capital that much of the activity of the Bank should be directed. To do so the Bank must pioneer with loans private capital is as yet justly too wary to undertake, while at the same time both Fund and Bank seek to develop those conditions in which trade and productive capital movements can be expected to prosper.

II. Powers

To help carry out these objectives, the Bank shall have the power to:

Make short-term and long-term loans to any participating government and to any political subdivision or business enterprise therein, providing the servicing of the loan is fully guaranteed by the national government.

To assure the most effective use of the Bank's resources it would probably be desirable to permit the extension of long-term financial aid to any government only after certain conditions are made. These conditions might be as follows:

(a) First, it would have to be reasonably certain that funds cannot be borrowed by the government in question from private investors except at high rates of interest. The Bank should carefully avoid competing with private investors when private investors are willing to invest or lend at reasonably low rates of interest. It will doubtless be possible for a number of the governments to borrow from foreign investors at low rates of interest, but for many of the countries such borrowing will be impossible until confidence is reestablished in the stability of the currency and in the social and economic stability of the borrowing countries.

(b) A second condition might well be that the loans can be made only after a careful study and written report has been made by a competent committee on the merits of the project and the loan. This condition would prevent hastily conceived action and also provide a record for the basis of any action taken by the Bank. It is a procedure which would be followed in most cases by the Bank anyhow, but because of the non-profit nature of the organization and the fact that it is a cooperative undertaking, such studies and reports are especially important.

(c) A third condition might be that financial aid should be forthcoming only when the committee's report definitely indicates that the loan would serve directly or indirectly to permanently raise the standard of living of the borrowing country. This provision would seem to be desirable in order to avoid loans that would finance armaments or loans that would permit careless budgetary practices, or loans to meet a deficit created by unwise fiscal policy. Unless a loan is productive in a broad and significant sense, it would seem better that the borrowing country should not be able to make the loan. For it to do so would in such case only increase its difficulties later on, and also defeat the purposes for which the Bank would have been established.

An exception to the above could, of course, be emergency relief loans. Immediately after the war there unquestionably would be need for provision of food and clothing and services which are definitely of relief character. Such financial aid would be vitally necessary in many countries to prevent social deterioration and political disruption as well as on purely humanitarian grounds. Where such financial assistance is given in the form of a loan and hence financed by the Bank it would seem just that the rate of interest charged should be only nominal.

(d) <u>Another condition of the loan that would seem to be necessary is that the funds borrowed are not to be used for purposes of repayment of an old loan.</u> Unless some such requirement is imposed the funds of the bank will be sought too frequently for purposes of bailing out defaulted bondholders. Nor would a refunding loan seem to fall in the category of productive loans. What the Bank is interested in is in expanding production, not in assuring past investors of the security of their investments.

Nonetheless, there will be cases in which a refunding loan at a low rate of interest might be of considerable help in relieving pressure on the country's budget. Consideration might be given to the possibility of permitting loans for that purpose under such circumstances providing four-fifths vote of the board of directors is obtained. However, once this possibility exists it would open the door for sluicing away a large part of the Bank's assets in loans which would contribute only remotely if at all to the objectives of the Bank.

Finally, <u>loans should be made only at low rates of interest with the schedule of repayments varying with the project.</u> The conditions of the loan ought never to be such as to impose a burden on the borrowing government either on its budget or on its balance of payments situation, which creates economic difficulties for that country. The lower the rate of interest the less difficulty will the country have in repaying the loan and the less risk will there be in making such loans. Low interest rates will have the effect of encouraging countries to borrow for productive purposes and make it possible at the same time for them over a course of years to build up their credit and thus encourage private investment. The greatest contribution that this Bank could make toward world recovery is that it could go a long way toward strengthening monetary systems of certain countries and increase the productivity of those countries, and thereby stimulate the flow of capital from private sources to those countries. An American corporation, for example, will much more readily undertake to finance the construction and operation of a plant in a foreign country if it feels that there are no undue burdens on the balance of payments imposed on the country and if, further, it sees concrete evidence of increasing productivity of that country arising from funds borrowed at low rates of interest and for long terms.

The gain that the United Nations would hope to obtain from the extension of long-term credits obviously does not rest in the interest payments that will be received. The gain is of a much more important character. It is the increased productivity, the heightened standard of living and improved well-being of the United Nations that would be reflected in increased trade and higher level of business activity everywhere. These desired goals can be attained more easily if the interest rates charged on loans are kept lower and if further the terms of payment are made such as do not bear too heavily on the borrowing country. It would be a grave error if the loans to the member nationals were to be evaluated according to commercial private banking principles. There are a number of reasons why the mere ability to pay the highest interest rate does not reflect the best international use for capital under conditions which will prevail during the post-war decade. That does not, of course, mean that loans can be made irrespective of a careful evaluation of their productivity. On the contrary, it is hoped that loans will be based on more careful studies of their utility than has ever been true with most private investments made to foreign countries. But it does mean that the studies of the merits of an investment is taking proper cognizance of the economic, social and political ramifications involved in the particular circumstances of any given loan.

Whenever possible the Bank should guarantee loans made by private investors, instead of making the loans directly, provided:

(a) The rate of interest is not in excess of (say) 4 percent;

(b) Not more than 80 percent of the principal and 50 percent of the interest is guaranteed;

(c) The loan is not for the purpose of repayment of an old loan.

In order to stimulate the flow of private capital and also to make the Bank's capital go as far as possible, it would be desirable wherever possible for the Bank to utilize the method of guaranteeing loans made by private investors instead of making the loans directly. This does not mean that the Bank would take the greater portion of the risk but in return for that it could make certain that the loan would be made under conditions and terms which received its approval. It would seem that such terms should include a low rate of interest probably not to exceed 3 or 4 percent. As stated above, the lower the rate of interest the less likely will there be a default. The difference, for example, between a 3 percent rate of interest on a 25-year loan and a 5 percent rate of interest on a 15-year loan is large. A country borrowing, say, $50 million for a 15-year period at 6 percent interest with straight line amortization would have to raise $ million a year for its budget and burden its balance of payments with that amount compared with $ million a year on its budget and balance of payments if the loan were at 3 percent and for a 25-year period. Another reason for a low rate of interest is not to encourage private capital from being reckless in the kind of loans it wishes to undertake. With the rate of interest high and with the government sharing a large part of the risk, there may be a tendency for loans to be made for purposes and under circumstances which in the long run would have unsatisfactory consequences.

For much the same reasons it would seem desirable for the Bank not to guarantee all the loan or service charges but to limit its guarantee to a maximum say 80 percent of the principal and 50 percent of the interest. There should, of course, be flexibility in this arrangement with broad authority left to the Bank to adjust the terms according to what it regarded to obtain the best results.

The provision that the loan should not be for the purpose of repayment of an old loan is based on considerations similar to those discussed a few pages back.

<u>No extension of credit should be extended by the Bank to any country, the National government of which is in whole or partial default of a foreign loan, unless</u>:

(a) The defaulted loan was made between Allies in a common war, or

(b) The defaulted government has agreed to renew service of the defaulted debt on a basis worked out by a special committee appointed by the Bank for that purpose, or

(c) Ninety percent of the member votes approve the loan.

If governments in default were made eligible for loans, again the danger would exist that the funds of the Bank might be used for the benefit of old bondholders and creditors rather than for the purpose of increasing the standard of living or productivity or trade of the borrowing nation. On the other hand, there are many countries in default and a number of them may be the very ones in need of financial aid. It would seem, therefore, that they should not be excluded from the possibility of borrowing provided certain conditions are present. For example, the loan in default may have been made by the Allies in a common war. This would apply, for example, to the British, French debts to the United States. It would seem that such loans because of their character and large magnitude should be excluded from the limitation.

A second condition, and one that has great possibilities for good and some possibilities for evil, is that a loan might be permitted to a government in default provided that government has agreed to renew the service of the defaulted debt on a basis worked out by a special committee appointed by the Bank for that purpose. A splendid job could be done in facilitating debt adjustments. The committee could approach the problem with a great deal more objectivity than could be true of a bondholders' committee representing the creditors and working with a committee representing the debtors. It could in its recommendations take a broader point of view and one that might well leave both the debtor and creditor nation better off than would be the case if a debt adjustment were to be obtained either as a result of political pressure of one kind or another, or because of an inducement offered to the defaulting government in the shape of a new loan to be made in effect only if the bondholders give their approval to the terms of adjustment.

With a committee of the Bank making the recommendations the loan could be forthcoming if the defaulting government accepted the committee's recommendation of terms of adjustments irrespective of whether the bondholders did or did not. As it is now the bondholders are in a position frequently to prevent the government from extending any credits on the grounds that they are not satisfied with the terms of adjustment offered by the defaulting government.

In some cases it might be extremely difficult to work out an adjustment with the defaulting government and it might be desirable in such cases to still permit a loan to be made, provided almost all of the member votes approve the loan. It might, therefore, be feasible to permit loans to the defaulting governments provided 90 percent of the member votes approve the loan.
<u>Loans made for the purpose of providing metallic reserves or otherwise strengthening monetary systems of the borrowing country should bear lower rates of interest and longer terms of repayment than loans made for other purposes</u>.

There will doubtless be opportunities to make loans for the purpose of providing metallic reserves or otherwise strengthening the monetary systems of the borrowing country. These loans could have a very salutary effect both because they would help promote monetary stability and would encourage the flow of private capital. Loans of that character should, it seems, bear a specially low rate of interest for three reasons. In the first place, such loans do not yield profits to the borrowing country of a character which are easily measurable. The charge on the budget of the servicing of the loan is a burden that can be justified only on general grounds. The encouragement to make loans for such purposes would be greater were the interest rate very low. Secondly, it would help defeat the purpose of the loan if high interest rates were charged, inasmuch as the burden caused by the loan would in that case tend to vitiate rather than to strengthen the benefits the loan might otherwise have. Finally, it might be said that in many cases the risk involved in lending metallic reserves for a monetary system under proper circumstances are less than other types of loans. For these reasons it would seem that an interest rate even as low as 1 percent on loans of metallic reserves for strengthening the country's monetary system might be in order.

Note Issuing Power.

To increase its resources, the Bank is given the authority to issue its own non-interest bearing currency notes. The notes might be made redeemable on demand in gold. The security for these notes should be the obligations of the participating governments or those of an intergovernmental corporation adequately secured, equal to 100 percent of the note issues, provided there is maintained in the Bank a gold reserve of 50 percent of the note issue. The provision that the obligations of any participating government shall not constitute backing for more than 10 percent of the note issue, is included to give added strength to the note issue.

Through its power of note issue, the Bank can substantially increase its cash resources. There could hardly be much question as to the soundness of the notes in view of the security required behind each note. The notes would be secured by 100 percent obligation of the borrowing country, plus 50 percent gold reserves, plus all other assets of the Bank, including obligations of all participating Governments. The notes should be as good as gold and should serve as a supplementary means of international payments.

The reason for suggesting that the Bank should be given the authority for the creation of a new currency unit lies chiefly in the fact that such authority would have, as indicated above, the effect of substantially increasing the loanable funds at the Bank's disposal.

A New International Currency

We frequently hear expressed a desire or hope for a new international currency, but the specific nature of the new currency is never described, nor are the gains that are presumed to result from such a currency ever stated in meaningful language. They are either taken for granted or referred to only in the vaguest of generalities. So much misunderstanding of the nature and utility of a new international currency seems to prevail that it is probably worth attempting to indicate the limits of usefulness possessed by such a currency. The disinterested reader can omit the next few pages.

There are some persons who seem to think that all foreign exchange problems would be solved if only all countries adopted the same international unit for use in international transactions. A little thought will demonstrate how absurd that belief is. The fact that Canada adopted a "dollar" unit containing 100 cents and having the same de jure gold content as the United States dollar, did not prevent the adoption of foreign exchange controls in Canada nor did it keep the United States dollar-Canadian dollar exchange rate from moving, any more than did Australia, South Africa and New Zealand, by adopting the same unit as England, prevent the value of the currencies of those countries from changing in relation to the British £ sterling. There are innumerable instances of different currency units keeping the same value, in terms of each other, for many years; and other instances of similar currency units beginning with identical values and only to have those values change greatly. Thus, the pound sterling hovered around $4.86 for twenty years (1893-1914), and the Swiss franc was about 20 cents for forty years; whereas, the exchange rates between the British £ and Australian £ and New Zealand £ and the Egyptian £ have moved greatly notwithstanding the fact that to begin with they all were the same unit, not only in designation--pound sterling--but in the sense that their value was 1 to 1.

The value of any currency in terms of any other country is a consequence of a complex of monetary and economic forces, changes in these forces influence the value of one currency in terms of others. The adoption of a new international currency would not modify those forces one whit. If all of the Western Hemisphere were to adopt the "dollar" as their own unit of currency, it would not be long before it would be necessary to distinguish from the "U. S. dollar", the "Mexican dollar", the "Colombian dollar", etc., because the exchange rates between those currencies had moved away from the 1 to 1 ratio. In fact, even now there are a number of "dollars" in use in the foreign exchange systems of the American Republics. The adoption of the same unit of currency no more eliminates foreign exchange problems than would the general adoption of Esperanto solve international political problems or no more than does the use of a common language, e.g. Spanish, eliminate international political problems between all Spanish-speaking nations.

Occasionally, one hears expressed the view that if only there could be created some unit of currency that could be universally used in trade--"a trade dollar" or "export dollar", or any unit with a new name--considerable advantages in trade and other international transactions would result. Unfortunately, this view is fallacious. The obstacles to trade do not lie in the fact that different countries use different units of currency. Insofar as currency has anything to do with obstructing trade, it is the scarcity of foreign exchange and the variations in exchange rates which are responsible. Neither of these two obstacles to trade will be dissipated by the adoption of a new international unit of currency. There are, it is true, possibilities of developing machinery which will make foreign exchange more plentiful to countries that lack adequate foreign exchange, and there is also machinery which may be developed to reduce the fluctuation in exchange rates. The proposal here made for the Fund and the Bank is designed to help achieve those very objectives among others. Neither proposal involves, or needs, or is dependent upon the adoption of an international unit of currency.

We already have an international medium of exchange, namely, gold. An ounce of gold .999 fine is the same in United States as it is in China or South Africa or Iceland. Any exporter or importer or banker or investor can liquidate a monetary debt with gold just as easily as would be possible with a new international unit. Such difficulties as exist in the use of gold as a medium of international exchange lie in difficulties imposed by war conditions. In peace time nothing could be simpler than to send or receive gold, or send or receive dollar or other exchange convertible into gold.

Some who clamor for a new international currency to replace gold would concede this, but claim gold is too expensive to be used. This is quite another matter. It may be possible to develop a satisfactory international medium of exchange that costs less to produce than more gold, but certainly not significantly less than gold already in monetary stock. It is important to remember in thinking about this subject that the monetary gold stock of the country <u>has already been paid for</u>. <u>It is very inexpensive to use the gold already in monetary stocks</u>. Even the cost of shipping from one country to another can be avoided through development of earmarking. The only expense of using gold already mined is the small value that gold would have for industrial uses if it had no monetary value.

The situation is quite different with respect to further additions to the gold stock and more complex. Obviously there is a real cost as well as a monetary cost involved in mining and refining gold. Insofar as the gold would not be produced had it only commodity value, and insofar as the labor and material used in gold mining would be used for some other purpose, it is true that additions to our monetary gold stock is expensive. The solution to that, however, is simple--namely, just limit the addition of newly-mined gold to the world's monetary stock. This is not the place to discuss the method; suffice to say it is entirely feasible should it ever be deemed desirable. There are some advantages and disadvantages to the proposal, but it is entirely possible that the time may come when the advantages may outweigh the disadvantages. In any case, the utility of additions to the world's monetary stock is a separate question from that of use of existing stocks. There is no advantage in substituting a new medium of international exchange for existing gold--even if it could be done--and I am confident it could not be done. But it may be worthwhile giving the Bank note-issuing powers--based on some gold reserve--solely in order to make the world's monetary gold stock do more work, and at the same time help correct the maladjustments in its distribution.

To be sure, the United States already does just that when for one reason or another, by one method or another it increases its supply of currency and demand deposits. The only difference between what the United States (and virtually every other country) already does, and what it is proposed the Bank shall do is that in the United States note issues are regulated by the law of the country, whereas the proposed note issues of the Bank will be regulated by the by-laws of the Bank as drawn up by the member Governments.

The belief previously referred to as being held in some quarters that a common unit of currency will solve the world's foreign exchange problems, and help promote foreign trade in goods and services, and the international flow of capital does not concern itself with either the scarcity of gold, or its maldistribution. It seems to take the form of something much less intelligible. It assumes that sooner or later a new international unit will be adopted by many countries as a substitute for their own currency.

The belief that countries will replace their own currency in favor of a currency to be used by all, or by a group of nations, is based on a fundamental misunderstanding of the factors which determine the value of any currency. So long as most countries insist on shaping their own monetary policies so long will it be impossible to replace local currencies with a new international currency. The adoption of a common currency by several countries is possible only if they each surrender separate sovereignty in monetary and credit policies in favor of sovereignty exercised by one over all of them, or by an international organization. For example, it was impossible for the states in the American colonies to have a common currency with a common value until the United States was formed and the Federal Government given sole authority over currency. Even then scores of different bank notes existed, many of them with changing values, because the State rather than the Federal Government exercised sovereignty in matters of bank note issue. It was only until the Federal Government became supreme in the matter of all note issues that the United States was able to keep all its bank notes at par.

But, it may be asked, would not the use of a new international unit as a supplement to local currency facilitate international trade and finance? The answer is an unqualified "No".

A "trade dollar" or "Demos" or "Victor" or "what-have-you" unit of currency supplementing the United States dollar, whether of the same or different value, would no more help foreign trade than would the adoption of a new flag. The only difference in trade between Massachusetts and Texas and trade between Massachusetts and Mexico--aside from tariffs--is that in the first case both buyer and seller deal in dollars only, whereas in trade between Mexico and United States two currencies are involved--the Mexican peso and United States dollar. The supply of either currency to either country would be no different than it could be without it, therefore, the matter of supply and demand for currency can be ignored in this discussion. An importer, exporter, bank, or a tourist has simply to make conversions from one currency into another in his transactions. Were it possible to eliminate by use of an international currency unit the arithmetical labors involved in the conversions, it would indeed be a convenient device, though by no means a very important one. Unfortunately, however, the use of a new international currency unit does not obviate the necessity of calculating conversion values any more than does the use of gold in settling international transactions.

Let us, for example, consider the case of a tourist. As it is now, when an American travels to Mexico he converts his dollars into Mexican pesos, when he enters Colombia he converts his dollars into Colombian pesos, and when he goes to Brazil he converts his dollars into milreis, etc. Yet, if there existed a new international unit of currency he would be no better off; his purchases and sales would be consummated with no less inconvenience. On the contrary, he would have to make more calculations and more monetary adjustments in his price judgments. For example, upon leaving the United States he would have to convert his dollars into the new international unit and then when he came to Mexico he'd have to convert the international unit into pesos just as he would have had to do had he carried with him dollars instead of an international currency, since most prices in any country are expressed in terms of the local currency unit. Only this time, if he wanted to judge the value of an article tagged, say 50 pesos, he would have to make two mental conversions instead of one because most of his life he has been dealing in dollars and cents, not in a new international currency. Then when he enters Colombia he would have to again calculate conversions and again make the necessary mental adjustments in evaluating his purchases. It would be possible, of course, to have price tags or price schedules in shops and hotels frequented by tourists expressed in the international unit, but such a practice would be a nuisance to the seller and would be only a slight convenience to the buyer.

Nor does a buyer of imported goods purchase those goods in one country rather than in another because of ease of an arithmetical calculation. Where there is any difficulty and the seller meets with any sales resistance on this score, he can easily overcome it by quoting his price in the buyer's currency even if a bill is to be paid in seller's currency.

Is there then no advantage to be obtained from the adoption of a new international unit of currency aside from the advantage of increasing the bank's lending resources described earlier?

Yes, there is one advantage, though of minor importance. It is in the realm of economic research. A universally recognized international monetary unit of account would be helpful in the presentation of those statistical series which are pertinent to international comparisons and of use in discussions involving international comparisons of quantitative data measured in money terms. For many purposes and in many media it would be convenient to set up tables that involved summation of money values in more than one currency. It would also prove useful in statistical data involving comparisons of various money values over long periods of time. It would make easier certain significant comparisons in cases where values set in terms of a local currency which had undergone substantial changes in purchasing power relative to other countries.

Altogether, the introduction of a new currency unit would not be of sufficient importance to warrant its introduction at this time, were the Bank not to be established with note issuing power. But if it is to be established and given the authority to issue notes, what unit shall it be?

It would probably be preferable to adopt an entirely new unit. The adoption of a new international unit of currency of account would probably meet with little opposition, whereas an attempt to use any one of the existing currencies, such as dollars, sterling, or franc for that purpose, would be opposed on the grounds that it would seem to give the country possessing that currency some slight advantage either in international publicity or in trade. There are deemed to be some national prestige values and possibly slight economic gains in trade and financial transactions that accrue to a country having a currency that is widely used as an international unit of account. For that reason a new unit belonging to no country would be more welcome to most countries than the unit of any selected country.

Obviously, a new unit of currency would have to be defined. It would have to be fixed in terms of something, whether by international agreement or by general acquiescense, or unilateral action. To set the value of the new currency unit in terms of some existing currency has the disadvantage of subjecting the new unit to the variations of the currency to which it is tied and also raises the question of "favoritism". A unit of account does not have to be set in terms of gold. It could, of course, be set in terms of some commodity other than gold--tin, platinum or any material. It could even be set in terms of an average basket of goods or an aggregate of goods. But examination of the various possibilities will reveal that the only practical solution is to set the new currency unit in terms of a given physical volume of gold.

For convenience of arithmetical calculation it would probably be well to define the new unit as being equivalent to 14.62 grains nine-tenths fine. This would make the new unit worth 50 U. S. or 10 yuan or 2 s. at current rates of exchange and at present price for gold in the United States.

Conditions to be imposed on borrowers.

It is hoped that the Bank in making loans would impose no condition on a loan as to the particular country in which the proceeds must be spent. To do so would not be in accord with the objectives of the Bank and the principles which underlie its creation. A borrowing government should be able to spend the borrowed funds in any of the participating countries. The participating countries are all members of the Bank, and even where a country spends the proceeds of a loan in a single country the flow from that expenditure ramifies to other countries. Therefore, any restrictions on the source of expenditure should be made only where very special circumstances seem to justify such action.

One of the conditions that might be given consideration is the provision that no loans shall be made where the funds are to be used for military purposes or the acquisition of armaments. It would probably be easier to obtain agreement on the principle than on carrying it out. Difficulties of execution arise because, though a country may not be using the specific funds which it is borrowing for the acquisition of armaments, it may still be true that the borrowed funds may release other funds which could be used for that purpose. It would therefore be very difficult to know how far to proceed with this limitation. If a potential borrower were expending any portion of its budget on the purchase of armaments made wholly or partly abroad, it would be, in effect, using funds that if not so spent could be used for the purpose for which the loan is presumably requested. The logical result of a strict imposition of such a condition would be that no government spending funds on armaments would be eligible for a loan. Clearly, this would be carrying the matter too far, inasmuch as it would mean that virtually no government would be able to borrow. On the other hand, if the world conditions are such as to justify the expectation of continued peace, the Bank should have the privilege of refusing the loan if it is convinced the borrowing country is spending too much on armaments. Probably, it would be best to phrase the condition in such way as to provide the Bank with authority to withhold loans if it sees fit on the basis of a country's unreasonably large expenditure on armaments.

When a loan or credit is extended to a member country the Bank shall divide the loan into two parts. One part shall consist of local currency and the other of the international units.

The division shall be based upon an estimate of the portion of the loan that is to be spent at home and that portion which is to be spent abroad. The reason for this is, first, the Bank will have included in its assets local currencies. This provision would provide a channel through which the Bank could utilize those currencies easily. Secondly, there is no reason why a country borrowing from the Bank for a specific venture not for the purpose of strengthening the monetary system should accumulate foreign exchange as the immediate result of such a loan. A substantial part of most loans would probably take the form of local expenditures and therefore local currency would fill the need. If the Bank does not have an adequate amount of such currency it could purchase it from the Fund thereby replacing local currency in the Fund with international units or its equivalent in gold. Care would have to be exercised in estimating the amount of local currencies to be utilized to make certain that due allowance was made for the indirect effects on imports of increased domestic expenditure--particularly where the loan is large relative to the economy of the borrowing country.

An alternative method might be to have all the Bank's transactions made in international units, leaving the Fund to perform the function of exchanging those units for various local currencies when necessary. This would have the advantage of simplifying somewhat the activities of the Bank, and of delegating all the questions of exchange transfers to the Fund. It would, however, have the disadvantage of making it a little more difficult in some cases to utilize local currency assets of the Bank and the Fund.

The service of the loan could be either in the identical currencies borrowed or in the new international units or gold. If it is to be made in local currencies it might be that the Bank would have to bear the risk of exchange. It could avoid that risk if it wished by making the underwriting of the exchange risk by the borrowing government a condition of the loan. Whether such practice would be desirable depends upon the particular case considered.

The Bank would have to be given the authority to buy, sell, hold and deal in gold, and in the obligations and securities of any participating government, to act as a clearing house for funds, balances, checks, drafts, and acceptances for the account of participating governments or their fiscal agencies and accept, demand time custody of the deposits and accounts from the participating governments and their fiscal agencies and central banks. It should also have the authority to discount and rediscount bills and acceptances and other obligations and instruments of credit of participating governments and fiscal agencies and central banks, and finally to act as agent or correspondent for any participating government and for fiscal agencies, central banks and political sub-divisions.

In short, the Bank is to perform virtually the same services of the participating governments that a central bank performs for the banks within a country. To what extent the various categories of services would be used only experience would demonstrate. For many years, the activities of the Fund in servicing the member governments, or their fiscal agents, may be quite unimportant. On the other hand, it is possible that in time the Bank will become more and more useful to the member governments.

It is expected that the Bank would interfere as little as possible with the activities of private banks and would perform only those services which the private banks are unable for one reason or another to perform efficiently or which are not performed at all. An exception to the above would be the operations of the governments and central banks. These should be performed by the Bank irrespective of the method.

The Bank might be given authority to organize and finance an international essential raw material development corporation for the purpose of increasing the world supply of essential raw materials and assuring member countries of an adequate supply at reasonable prices.

There are a number of possibilities which exist for the development and proper distribution among nations of raw material sources. It may be that under the aegis of this Bank it would be possible to establish international corporations, government controlled, which would on the one hand promote the exploitation of natural resources in distant areas, and on the other hand, assure to the member governments a fair share of those resources at reasonable prices. It is too early to know what will happen to many of the colonies of European nations now in enemy hands that possess needed raw materials. There would doubtless be considerable opposition to the resumption of control of important sources of raw materials by any one nation. It may be that the problem of determination as to the sovereignty of particular areas invaded by the enemy would be simplified if some instrumentality were developed to provide for the exploitation and the distribution of the product among cooperative, intergovernmental lines. Under any such arrangement it would still be possible for private capital and managerial services to operate such resources with the international organization by virtue of some financial participation determining such major policies as price and national quotas of sale.

Were the Bank able to solve the problem of preventing monopoly of control of necessary raw materials, it will have made a large contribution toward removing one of the elements of friction among nations. Such an organization need not be created by the Bank, it could be a quite independent international undertaking. Yet being an international governmental institution operating for the benefit of all the members, and having large financial resources would seem to be an appropriate agency for the promotion and partial financing of international controls over raw material sources. On the other hand, it might be felt that the Bank is ill equipped to handle a task of that complexity and magnitude. That objection, however, would apply more to the management of a corporation than to supply a part of the necessary capital to the various ventures.

The advantage of having the Bank possess the authority to finance an international corporation of this character is the relative ease with which the financing could be accomplished if plans for such an organization were acceptable to the governments concerned. Unless there is an international agency such as the Bank to provide a substantial portion of the capital necessary to get an international corporation started, each of the countries would have to make separate appropriations possibly of rather substantial sums. There probably exists in many countries adequate authority to participate in an international enterprise of the kind described above but funds would not be available unless Congress or Parliament made special appropriations. If, therefore, a bank were to be able to provide part of the funds, the remainder to be obtained by public fluctuations from private investors, it might not be necessary to have the matter go before various legislative bodies.

Another possible advantage of having the Bank help finance the corporation instead of making it necessary for a specially created body to obtain all its capital from governments or public would be that there would then exist an independent inter-governmental organization equipped with personnel and sources of information which should be able to wield a desirable influence and provide a useful check on the operations of the corporation.

<u>The provision giving the Bank authority to organize and finance what might be termed an International Commodity Stabilization Corporation represents a departure similar to that discussed above in the Raw Material Corporation.</u> There is urgent need for the establishment of an agency owned by a number of interested governments which shall engage in activity having for their objective the stabilizing of the prices of important commodities. To develop a satisfactory working arrangement capable of evening up the gluts and scarcities of important commodities and raw materials--such as tin, rubber, cotton, coffee, wheat, corn--will prove to be a very difficult task. There are innumerable problems of great complexity involved in such an attempt. There are some who think it can be worked out. One of the obstacles is the provision of adequate financing arrangements. The purpose of including among the powers of the Bank the authority to organize and finance such an institution is to provide the vehicle for implementing a plan if one is developed that gives promise of being able to satisfy the need.

In view of the large sums of money that are likely to be involved and the large risks inherent in any such attempt, it seems desirable to (a) require that the Bank can organize and finance such an agency only if at least five governments participate directly in the management and operation of the corporation and subscribe to part of the capital of the corporation, and (b) that the corporation will undertake to stabilize the price of any specific commodity only with the consent of the Bank, and (c) the policy governing the operations of the corporation gives, in the opinion of the Board, proper weight to the interests of world consumers as well as producers.

It is presumed that if satisfactory plans could be worked out for the establishment of an international commodity stabilization corporation it would include as one of its most important functions the authority to purchase a selected commodity when the price rose above a selected level and sell when it rose below a pre-determined level. The amount of capital which a corporation attempting to carry out such a plan could absorb would be very great indeed. To help finance itself it could give its notes to the sellers of the commodity for part of the purchase price. The Bank could be given authority to discount these notes, provided the government of the country in which the seller of the commodity resided in question would endorse the note. In this way the activities of the corporation could be partly financed by the Bank without the Bank taking great risks. It also would make possible the sale of surpluses by governments who could not afford under other circumstances to finance the warehousing or purchasing of those surpluses.

Inasmuch as the Bank is an inter-governmental institution representing the interests of the peoples of member countries it would seem that it should make certain that the corporation lending large sums is operating under policies which protect the consumer as well as the producer. There might be a strong temptation in the corporation's operations to overlook the interest of the consumers and place the selling price of particular commodities at too high a level.

<u>To increase the potential resources of the Bank, authority should be given to it to rediscount with any government or fiscal agents or central bank bills, acceptances and other instruments of credit taken from the Bank's portfolio.</u>

Also the Bank should be able to issue or sell acceptances and obligations of the Bank in order to obtain assets for the purpose of the Bank.

Both of these latter provisions should provide potential resources adequate to satisfy any reasonable demands that the Bank might be called upon to supply. The operations of the Bank as the operation of any credit agency would have to be managed with an eye to building up the strength, the prestige and status of the Bank. The extent to which it can increase its capacity to undertake long-term financing and at the same time be able to take care of unusual situations, will be directly related to the care with which it exercises in the increase of its portfolio. On the other hand, it cannot be as cautious in its decisions as would be a commercial bank. It would be easy to operate on a very conservative basis. It is far easier, and of course far less risky, for a banker to say "no" to a demand than "yes." But in the case of the Bank it should never be forgotten that its primary purpose is to make loans that commercial banks would not, could not, or should not make except at very high interest rates. Hence, a banking policy characterized by caution and conservatism could easily defeat the purpose for which the Bank is to be created. If an error is to be made, it probably were preferable that the management err on the side of under-caution rather than over-caution. Yet the Bank must be built carefully and soundly if it is to endure and play an important role in the distant as well as in the immediate future. It is certain to prove to be a difficult task to steer between excess caution and excess liberality. Realization of this difficulty only emphasizes the necessity for selecting the most able men to manage the Bank; men with varied experience who are more than bankers in their outlook and less than college professors in their decisions.

III. Capital Structure

In order for the Bank to have resources adequate for the purposes for which it is presumably to be created, it should have very large sums available for loans. It is suggested that the capital stock be authorized up to $10 billion, consisting of 10,000 shares having a par value of $1 million each. The provision that only 50 percent of the issue price need be paid at the time of the subscription, and the further provision that one-half of the down payment can be in the currency of the participating country (the other half being in gold), should make it not too difficult for all of the United Nations to participate even though the shares have a par value of $1 million each.

The provision that each eligible government can subscribe to as many shares of stock as it wishes but must at least subscribe to a number of shares equal to 2 percent of its annual national income, is designed to permit small countries to participate as well as large and yet to prevent large countries from investing a small sum merely to obtain such benefits as participation yields without undertaking any of the responsibilities or risks that participation carries with it. Under that arrangement, for example, the United States would have to acquire at least $2 billion worth of shares, half of which would be paid for at the time of the subscription, whereas a country like Cuba, for example, would have to subscribe to only $20 million.

There is, however, the further provision that the maximum votes any country may cast is 25 percent of the total, irrespective of the number of shares it might own. The purpose of this provision is to prevent control of the Bank by any one government.

As with the Fund, there is the very important problem of control over the Bank. In the Bank as in the Fund, there is the necessity to give the country with larger participation a larger number of votes and yet to assure the small countries an influence in voting in excess of their necessarily small contribution. This might be achieved by giving each member of the Bank the authority to cast 50 votes plus one for each share of stock held. Thus the United States--assuming it were to subscribe $2 billion worth of shares--would have 50 votes plus 2,000, while Cuba would have 50 votes plus 20. It was thought that the country acquiring more shares should have a larger number of votes relative to the other countries than was true in the case of the Stabilization Fund, because the monetary risks involved in the Bank are much greater than those in the Fund. It is not expected that the Fund would experience great losses over a course of years, whereas there is no telling what losses the Bank would have to sustain. The difference in risk follows from the difference in character of the transactions undertaken by the Fund and by the Bank.

IV. Eligibility for Membership

By including the requirement that the participant be a member of the United Nations Stabilization Fund in effect includes all the requirements of membership in the Fund. It may well be that after discussion some of the eligibility requirements of the Fund may be dropped and yet may be desired for membership in the Bank. There does not seem to be any special reason why the requirements should be different in one case than the other, but such reasons may be revealed during discussions.

One reason for requiring that a member of the Bank be also a member of the Fund would seem to be that some countries would stand to gain most from membership in the Bank, and others from membership in the Fund. If a country were able to select the agencies membership in which it had most to gain, the more powerful and richer countries might prefer the Fund, while the less powerful countries, or those most in need of long-term capital assistance, might prefer membership in the Bank. The result might be that the Bank would start out with resources that are inadequate for its objectives, whereas the Fund would have more resources than necessary and, at the same time, would have its effectiveness diminished because of a smaller number of participants. The more participants there are in the Fund, the more effective it would be, whereas, the larger the subscriptions to the Bank, the more effective could be the Bank.

Inasmuch as the objectives of both the Fund and the Bank are such as to benefit all of the United and Associated Nations, either directly or indirectly, it would seem reasonable to expect them to be members of both, even though the direct benefits they might achieve might be allocatable to either one or the other agency.

In addition to having to be a member of the Fund there is the requirement indicated that the participants subscribe publicly to a "Magna Charta of the United Nations". This requirement is inserted with trepidation as it is not at all certain that the inclusion of such a requirement is appropriate. The Magna Charta constitutes a bill of rights of the peoples of the United Nations. A copy of this Magna Charta is appended. Public adherence to the policies expressed in the document would, I believe, be opposed by none since the document sets forth the ideal of freedom for which most of the peoples are fighting the aggressor nations and hope they will be able to attain and believe they are defending.

Examination of the document will reveal, however, that there are a number of countries which in their practices do not now give, and have not given, evidence that they subscribe to the principles contained therein. No country would probably wish to admit that they were not, however, willing to abide by those principles as soon as it was feasible and insofar as it was possible. Since the document merely calls for a public adherence to the principles, it would probably not prevent any of the United or Associated Nations from participating. The mere public announcement that they subscribe to those principles would be a great step forward in the struggle to obtain those rights for all the peoples. The inclusion of that provision would make clear to the peoples everywhere that these new instrumentalities which are being developed go far beyond usual commercial considerations and considerations of economic self-interest. They would be evidence of the beginning of a truly new order in the realm where it has hitherto been most lacking--international finance.

A final condition is that the members be at peace with other member countries. Any member that is held by two-thirds of the members of the Bank to have undertaken an act of aggression against any other member of the Bank shall forfeit its membership in the Bank.

The purpose of this requirement is two-fold. First, it would provide an additional motive for hesitating to undertake an act of aggression. As a deterrent, this last would probably be much less significant in the case of large countries than it would be in the case of small ones. There have been instances in the past decade in which the small countries have undertaken what are generally recognized as acts of aggression, where they might have hesitated to do so if the consequences of such act were to have been economic loss, loss of credit standing and loss of prestige, such as would follow from being dropped from two agencies, such as the Fund and the Bank, were they to have played the role that is expected of them, if they are established. The second reason would be to impose at once a form of economic sanction on an aggressor country, and by that act, to obtain for the non-aggressor nations whatever political and psychological advantages accrue from the public designation of an aggressor.

If other international agencies, political in character, are developed which would have the responsibility of determining the aggressor and apply economic sanctions, the authority of the Bank to do so would probably be much less important. Until such time, however, it might be helpful to include it in the requirement for membership in the Bank.

As an inducement to the countries to subscribe to the terms and conditions required of members, and as a penalty for not doing so, there is a provision that any government that withdraws or is expelled from the Bank loses its membership in the Fund and vice versa. In other words, the two agencies, the Fund and the Bank, have closely linked together in their adherence to the kind of policies set forth in their objectives and powers.

V. Management

As with the Fund it would seem that the most efficient method of management is to have the administration of the Bank vested in the Board of Directors with an executive committee appointed by the Board of Directors and the President of the Bank elected by the directors. Provisions for the selection of the officials of a Bank should be such as to assure a responsiveness of the Board of Directors to their respective governments and of the Executive Board to the Board members.

Also, regulations should be such as to permit the Executive Board to conduct as much as possible of the day-to-day operations, without the necessity of referring to the larger Board for decisions. Because of the importance that continued experience would have for the best functioning of the Board, it would be desirable to provide for long tenures of office for many of the Board members, and eligibility for reelection for the higher officials.

To stress the international character of the Board of Directors, and to avoid any possible affront to the dignity of member governments, it may be desirable to work out an arrangement for rotating the chairmanship of the Board of Directors.

To facilitate the operations of the Board, authority is given to permit the executive committee to exercise any specified powers provided those powers are set forth by four-fifths majority vote, and provided further that such powers shall be exercised only until the next formal meeting of the Board and only in a manner consistent with the general policies and practices of the Board.

Because of the very broad area of operations which the Bank would in time wish to undertake, it is thought that the Bank should be able to take advantage of special advisory committees appointed by the Board, the members of which may not be readily employed by the Bank.

It is further required that two-thirds of the majority vote of the Bank shall be required for making long-term loans. It is thought desirable to have more of a majority acquired for this purpose because it would seem that if almost half of the members of the Board disapprove of a loan that in itself would constitute adequate justification for not undertaking it.

VI. Distribution of Profits

The Bank should have substantial earnings almost from the beginning of its operations. To build up a surplus in the Bank, provisions should be made for the distribution of not more than 75 percent of the profits, and possibly less, until the surplus shall be equal to a substantial portion of the paid-in capital, possibly 20 percent.

To further strengthen the Bank's assets, it might be possible to work out an arrangement whereby each country were to receive its profits in the form of its own currency. This would provide an opportunity for the Bank to reduce greatly its holdings of local currency. So long as the Fund is in existence, there is no need for the Bank to operate in anything but gold and international units.

VII. Reports and Information

As with the Fund, the Bank's ability to conduct its affairs wisely will depend in large part on the competence of the economic analyses and information available to it. Because of its anticipated close liaison with the Fund, it would have available the comprehensive current information that the Fund would use in the performance of its duties. But the Bank would need additional special studies and special reports appropriate for its particular functions. It should have the necessary authority to obtain such studies and to require such reports from the member governments. It should also have the authority to send the experts into the field to make surveys, studies and investigations necessary for the proper evaluation of any project in which it already has a financial interest, or in which it is requested to help finance.

Bank for Governments. The Bank is definitely not an institution to be operated for the purpose of acquiring profit. It will, of course, have to undertake risks which no commercial bank would or could afford, and its activities furthermore are related to problems of monetary, financial and commercial policy of foreign governments. Hence, it is fitting that the Bank should deal only with governments or their fiscal agents.

The Bank should have authority to engage in financial economic studies and public reports thereof. This should become an important function of the Bank both because it would give an opportunity for the people in various countries to evaluate the work of the Bank and also because it could well serve as a channel for information and education on matters pertinent to the Bank's operations. As time went on, and if and when the importance of the Bank grew, these studies would become an important medium for analysis and discussion of economic developments the world over.

Treasury Department
Division of Monetary Research 313

Date May 8 19 42

To: Miss Chauncey

From: Mr. White

The Secretary wanted to see this.

314

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE May 8, 1942

TO Secretary Morgenthau

FROM H. D. White

Subject: Financial Implications of the Proposed Pooling of Canada's War Production through Washington.

Messrs. Clark, Carswell, Wrong and Plumptre of the Canadian Government met yesterday afternoon in my office with Generals Aurand and Maloney and representatives from State, Lend-Lease, Board of Economic Warfare and this Division, to discuss the possible effects, on Canada's dollar position and use of Canadian production facilities, of the proposed pooling of Canada's war production through the Joint Munitions Assignment Board in Washington. The discussion brought out the following interesting facts:

1. War production of Continental United States is being assigned by the Joint Munitions Assignment Committee in Washington, without regard to financing according to strategic needs. The Joint Assignment Committee in London, on which there is an American representative, has complete responsibility for assigning munitions within the British Empire.

2. The present arrangement of assigning Canadian production through London has given rise to a number of difficulties largely because many Canadian factories have orders for the identical item from each of the Governments of Canada, the United Kingdom and the United States. The proposal that Canadian production be pooled through Washington has come from the British and Canadians and not from the United States side. However, General Aurand strongly favors the proposal.

3. The Canadians feared that the proposed pooling arrangement would mean the United States Government would order less in Canada and Canada would therefore receive fewer U. S. dollars. General Aurand assured them that the U. S. Army would not order less, but more, even if the pool does dispose of the finished munitions.

4. The problem of financing arises only in those cases where goods produced in Canada on British orders

would be diverted to non-British Empire countries, because there appears to be no doubt that goods ordered in Canada by England, and assigned to the Empire will be financed by arrangements between Canada and British Treasury. General Aurand believes that the best possible utilization could be made of the resources and finished munitions of both countries by the pooling proposal. He has confidence that the financial problem, which should not be allowed to interfere, can be settled by the Treasuries.

Dr. Clark is pleased and is now satisfied that the new arrangement will not adversely affect Canada's dollar position.

I presume that Canada will enter the pooling arrangement.

It looks to us as though the new arrangement will increase Canada's U. S. dollar receipts. There is a possibility that Canada will be producing progressively more on United States account than on British account. This may mean that the United States will be paying Canada more dollars, while Canada will be contributing less to England, or, to state it differently, that England will be getting more from us under lend-lease and less from Canada under the recently-announced Canadian gift to Britain.

The Treasury should watch the situation carefully and we propose to ask General Aurand to keep us informed as to orders and deliveries on U. S. Government contracts in Canada. We may also have to obtain data on orders and deliveries on British and Canadian Government contracts placed in Canada if we are to be able to explain what is happening in the three-way financing arrangements.

MAY 8 1942

Dear Mr. Chen:

I am glad to receive your letter of March 22, 1942 and appreciate your kind words regarding the part which the United States Treasury has played in extending aid to China.

As you know, I am happy to have had the opportunity to be of some assistance to the Chinese people whose valor and courage have always had my deep esteem. May I congratulate you again on the prompt repayment of the Woodoil Loan in spite of the very difficult conditions under which you worked.

I hope this letter finds you in the best of health.

Sincerely yours,

(Signed) H. Morgenthau, Jr.

Secretary of the Treasury.

Mr. K. P. Chen,
Chairman, Stabilization
Board of China,
Chungking, China.

File N.M.C.
cc - Dr. White

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May 1, 1942

The Honorable Henry Morgenthau, Jr.
Secretary of the Treasury
Department of Treasury
Washington, D. C.

Dear Mr. Secretary:

I take pleasure in enclosing herewith letter addressed to you by Mr. K. P. Chen which came in care of a personal friend of Mr. Chen who has just arrived from China.

With my kindest personal regards,

Sincerely yours,

S. D. Ren
Vice-President

SDR:d
enc.

K. P. CHEN
PRIVATE OFFICE

Chungking
March 22, 1942

The Hon. Mr. Henry Morgenthau
Secretary
Department of Treasury
Washington, D. C.

Dear Mr. Morgenthau:

I have just had the pleasure of informing you through the cable that the Universal Trading Corporation has been authorized to hand over to the Export-Import Bank the last instalment in repayment of the Woodoil Loan of February 8, 1939. As sufficient funds have accumulated on hand, the Universal is thus happily enabled to discharge its obligation ahead of the stipulated time.

I would like to take this opportunity to thank you once more for the great pleasure which our association has given me. I am gratified that fortune has enabled me to make good my old promise to you.

For the past three years I have been watching with ever keener interest and admiration the consistent demonstration of your statesmanship in the prosecution of America's policy of financial assistance to China which you initiated. Needless for me to say how deeply appreciative our people are of the abiding friendship of your nation. Events of the world have lately developed to make China and America comrades in arms, and I have not the least doubt that the two countries, bound by a common determination and objective, will ultimately see the triumph of liberty over organized barbarism.

With compliments and regards,

Sincerely yours,

K. P. Chen

C
O
P
Y

DEPARTMENT OF STATE

WASHINGTON

May 8, 1942

In reply refer to
FD 846K.5151/4

The Secretary of State presents his compliments to the Honorable the Secretary of the Treasury and encloses copies of telegram no 24, dated May 8, 1942, from the American Consulate, Suva, Fiji Islands, concerning "plan of procedure outlined for the disposal of United States paper currency and official drafts".

Enclosure:

From Consulate, Suva,
no. 24, May 8, 1942.

Copy:lc:5/9/42

BR
This telegram must be paraphrased before being communicated to anyone other than a Governmental agency. (BR)

Suva

Dated May 8, 1942

Rec'd 8:45 a.m.

Secretary of State,

Washington.

24, May 8, 1 a.m.

Your 20, April 27, 1 p.m.

Please inform treasury "plan of procedure outlined for the disposal of United States paper currency and official drafts welcomed by Bank of New South Wales and Bank of New Zealand.

If Treasury approves the proposed procedure will be adopted also for Bank of New Zealand except that bank (*) United States paper currency (but not drafts) it may cash to Bank of New South Wales for cancellation and delivery to this office.

The new local exchange rates when fixed and the date of their adoption will be telegraphed."

ABBOT

BR

(*) Apparent omission.

Copy:lc:5/9/42

CORRECTED COPY

BR
This telegram must be paraphrased before being communicated to anyone other than a Governmental agency. (BR)

Suva

Dated May 8, 1942

Rec'd 8:45 a.m.

Secretary of State,

Washington.

24, May 8, 1 a.m.

Your 20, April 27, 1 p.m.

Please inform treasury "plan of procedure outlined for the disposal of United States paper currency and official drafts welcomed by Bank of New South Wales and Bank of New Zealand.

If Treasury approves the proposed procedure will be adopted also for Bank of New Zealand except that bank will pass on United States paper currency (but not drafts) it may cash to Bank of New South Wales for cancellation and delivery to this office.

The new local exchange rates when fixed and the date of their adoption will be telegraphed."

ABBOT

RR

Copy:bj:5-12-42

TREASURY DEPARTMENT

INTER-OFFICE COMMUNICATION

DATE May 8, 1942

For Miss Chauncey

TO Secretary Morgenthau

FROM Mr. Dietrich

Official sales of British-owned dollar securities under the various vesting orders since February 19, 1940:

	No. of Shares Sold	$ Proceeds of Shares Sold	Nominal Value of Bonds Sold	$ Proceeds of Bonds Sold
Apr. 20	-	-	-	-
21	-	-	-	-
22	-	-	-	-
23	-	-	-	-
24	-	-	-	-
25	-	-	-	-
	-	-	-	-
Sales from Feb.22,1940 to Apr. 18, 1942	9,847,610-1/6	281,858,763	45,648,016	37,474,216
Sales from Feb.22,1940 to Apr. 25, 1942	9,847,610-1/6	281,858,763	45,648,016	37,474,216

TREASURY DEPARTMENT

INTER-OFFICE COMMUNICATION

DATE May 8, 1942

TO Secretary Morgenthau
For Miss Chauncey

FROM Mr. Dietrich

Official sales of British-owned dollar securities under the various vesting orders since February 19, 1940:

	$ Proceeds of Shares Sold	$ Proceeds of Bonds Sold	Total	
Apr. 20	-	-	-	
21	-	-	-	
22	-	-	-	
23	-	-	-	
24	-	-	-	
25	-	-	-	
	-	-	-	
Sales from Feb.22,1940 to Apr. 18, 1942	281,858,763	37,474,216	319,332,979	
Sales from Feb.22,1940 to Apr. 25, 1942	281,858,763	37,474,216	319,332,979	319,332,979
$ proceeds of non-vested securities sold Apr. 13, 1942 - April 18, 1942			300,000	
$ proceeds of non-vested securities sold Sept. 1, 1939 - April 11, 1942			246,500,000	
$ proceeds of non-vested securities sold Sept. 1, 1939 - April 18, 1942			246,800,000	246,800,000
			GRAND TOTAL	566,132,979

Jan. 7, 1942 - Cash Dividend on 156 Shares	$ 61
Jan. 9, 1942 - Partial Liquidating Dividend	125
9 Units sold from Aug. 18, 1941 - April 25, 1942 for	42
11 Shares Stock Dividend sold Aug. 18, 1941 - April 25, 1942 for	123
56,007 Rights sold from July 24, 1941 - April 25, 1942 for	102,938

D

TREASURY DEPARTMENT

INTER-OFFICE COMMUNICATION

DATE May 8, 1942

TO Secretary Morgenthau

FROM Mr. Dietrich

For Miss Chauncey

Official sales of British-owned dollar securities under the various vesting orders since February 19, 1940:

	No. of Shares Sold	$ Proceeds of Shares Sold	Nominal Value of Bonds Sold	$Proceeds of Bonds Sold
Apr. 27	-	-	-	-
28	-	-	-	-
29	-	-	-	-
30	-	-	-	-
May 1	-	-	-	-
2	-	-	-	-
	-	-	-	-
Sales from Feb.22,1940 to Apr. 25, 1942	9,847,610-1/6	281,858,763	45,648,016	37,474,216
Sales from Feb.22,1940 to May 2, 1942	9,847,610-1/6	281,858,763	45,648,016	37,474,216

TREASURY DEPARTMENT

INTER-OFFICE COMMUNICATION

DATE May 8, 1942

TO Secretary Morgenthau

FROM Mr. Dietrich

for Miss Chauncey

Official sales of British-owned dollar securities under the various vesting orders since February 19, 1940:

	$ Proceeds of Shares Sold	$ Proceeds of Bonds Sold	Total	
Apr. 27	-	-	-	
28	-	-	-	
29	-	-	-	
30	-	-	-	
May 1	-	-	-	
2	-	-	-	
	-	-	-	
Sales from Feb.22,1940 to Apr. 25, 1942	281,858,763	37,474,216	319,332,979	
Sales from Feb.22,1940 to May 2, 1942	281,858,763	37,474,216	319,332,979	319,332,979
$ proceeds of non-vested securities sold April 20, 1942 - April 25, 1942			400,000	
$ proceeds of non-vested securities sold Sept. 1, 1939 - April 18, 1942			246,800,000	
$ proceeds of non-vested securities sold Sept. 1, 1939 - April 25, 1942			247,200,000	247,200,000
			GRAND TOTAL	566,532,979

Jan. 7, 1942 - Cash Dividend on 156 Shares	$ 61
Jan. 9, 1942 - Partial Liquidating Dividend	125
9 Units sold from Aug. 18, 1941 - May 2, 1942 for	42
11 Shares Stock Dividend sold Aug. 18, 1941 - May 2, 1942 for	123
56,007 Rights sold from July 24, 1941 - May 2, 1942 for	102,938

BRITISH AIR COMMISSION
1785 MASSACHUSETTS AVENUE
WASHINGTON, D. C.
TELEPHONE HOBART 9000

PLEASE QUOTE
REFERENCE NO. ____________

With the compliments of British Air Commission who enclose Statement No. 32 - Aircraft Despatched - for week ended May 5, 1942.

The Honourable Henry Morgenthau, Jr.
Secretary of the Treasury
Washington, D. C.

May 8, 1942.

MOST SECRET

STATEMENT NO. 32

AIRCRAFT DESPATCHED FROM THE UNITED STATES
DURING WEEK ENDED MAY 5th, 1942

TYPE	DESTINATION	ASSEMBLY POINT	BY SEA	BY AIR	FLIGHT DEL'D FOR USE IN CAN.
BELL					
Airacobra	U.K.	U.K.	3		
BOEING					
Boston III	U.K.	U.K.	5		
CESSNA					
AT 17 Crane IA	Canada	Canada			4
CURTISS					
Kittyhawk IA	Middle East	Port Sudan	28		
	New Zealand	Wellington	7		
CONSOLIDATED					
Liberator II	U.K.	Canada en route		2	
LOCKHEED					
A 29 Hudson III A AC 5	Canada	Canada			1
A 29A AC 151	U.K.	Canada en route		1	
Ventura	U.K.	Canada en route		5	
Ventura	Canada	Canada			2
GRUMMAN					
Martlet II	U.K.	U.K.	1		
NORTH AMERICAN					
Mustang	U.K.	U.K.	59		
TOTALS			103	8	7

British Air Commission

May 8th, 1942.

BRITISH AIR COMMISSION

1785 MASSACHUSETTS AVENUE
WASHINGTON, D. C.

TELEPHONE HOBART 9000

PLEASE QUOTE
REFERENCE NO.

With the compliments of British Air Commission who enclose weekly Statement No. 50, covering Aircraft Flight Delivery as at May 6, 1942.

The Hon. Henry Morgenthau, Jr.
Secretary of the Treasury
Washington, D. C.

May 8, 1942.

MAY 6, 1942

CONFIDENTIAL REPORT
REP. NO. B-56

LOCATIONS OF CLEARING FLIGHT DELIVERY AIRCRAFT -- WEEKLY REPORT NO. 50

1. LIBERATOR II off Contract B-677
   (A) Never taken by A.A.F.
   55 delivered to U.K.
   5 delivered to M.E. (1 crashed in Africa)
   5 at Montreal
   65

   (B) Taken and Returned or Kept by A.A.F.
   3 delivered to U.K.
   1 at Bluie West 1
   2 in Ferry Service (delivered to Montreal)
   1 at Gander
   11 at Montreal
   2 at Detroit
   1 en route Detroit
   3 to be returned
   6 retaken by A.A.F.
   44 kept by A.A.F.
   74

2. HUDSON V (LONG RANGE) off Contract A-1749
   173 delivered to U.K.
   39 delivered to Debert
   3 at Montreal (for Debert)
   1 at Detroit (for Debert)
   2 under repair
   7 crashed (2 in U.S., 5 after export)
   225

3. HUDSON III (LONG RANGE) off Contract A-68
   211 delivered to U.K.
   4 at Montreal
   19 for U.S.A.A.F. Familiarization Program
   1 under repair
   10 crashed (1 in U.S., 9 after export)
   245

4. VENTURAS off Contract A-344
   (A) LONG RANGE
   8 delivered to U.K.
   1 at Goose
   9 at Gander
   12 en route Gander
   59 at Montreal (including 1 for West Palm Beach)
   91 at Detroit (including 15 for West Palm Beach)
   10 en route Detroit
   3 at West Palm Beach
   1 at Wright Field
   2 at Long Beach
   1 crashed (in Canada)
   197

   (B) SHORT RANGE
   8 at Montreal
   4 at Detroit
   1 en route Detroit
   2 at West Palm Beach
   1 at Long Beach
   16
   (10 shipped to U.K. by Sea
   26 Total reported away from plant)

S. SECRET - BRITISH MOST SECRET

MAY 6, 1942

CONFIDENTIAL REPORT
REF. NO. [illegible]

LOCATIONS OF [illegible] FLIGHT DELIVERY AIRCRAFT -- WEEKLY REPORT NO. [illegible]

1. LIBERATOR II a/c Contract F-677
   (A) Never taken by A.A.F.
   55 delivered to U.K.
   5 delivered to M.E. (1 crashed in Africa)
   5 at Montreal
   65

   (B) Taken and Returned or Kept by A.A.F.
   3 delivered to U.K.
   1 at Bluie West 1
   2 in Ferry Service (delivered to Montreal)
   1 at Gander
   11 at Montreal
   2 at Detroit
   1 en route Detroit
   3 to be returned
   6 retaken by A.A.F.
   44 kept by A.A.F.
   74

2. HUDSON V (LONG RANGE) a/c Contract A-1748
   173 delivered to U.K.
   39 delivered to Debert
   3 at Montreal (for Debert)
   1 at Detroit (for Debert)
   2 under repair
   7 crashed (2 in U.S., 5 after export)
   225

3. HUDSON III (LONG RANGE) a/c Contract A-68
   211 delivered to U.K.
   4 at Montreal
   19 for U.S.A.A.F. Familiarization Program
   1 under repair
   10 crashed (1 in U.S., 9 after export)
   245

4. VENTURAS a/c Contract A-244
   (A) LONG RANGE
   8 delivered to U.K.
   1 at Goose
   9 at Gander
   12 en route Gander
   59 at Montreal (including 1 for West Palm Beach)
   91 at Detroit (including 15 for West Palm Beach)
   10 en route Detroit
   3 at West Palm Beach
   1 at Wright Field
   2 at Long Beach
   1 crashed (in Canada)
   197

   (B) SHORT RANGE
   8 at Montreal
   4 at Detroit
   1 en route Detroit
   2 at West Palm Beach
   1 at Long Beach
   16
   (10 shipped to U.K. by Sea
   26 Total reported away from plant)

. S. SECRET - BRITISH MOST SECRET

LOCATIONS OF OCEANIC FLIGHT DELIVERY AIRCRAFT -- WEEKLY REPORT NO. [illegible]

5. CATALINAS
(A) Off Contracts A-2267, F-210, A-37, ABR-28, SAB-78
104 delivered to U.K.
9 delivered to Singapore
27 delivered to Australia
8 at Dartmouth
3 in Bermuda
2 crashed (in Bermuda)
153

(B) PBN 5-A's off BDB Req. 10772
8 delivered to U.K.
4 at Montreal
12

6. LODESTARS off L/L Contract AC-53 BDB Req. 1040
(A) C-59's
6 departed Miami or W.Palm Beach:
1 at Miami
3 taken by A.A.F.
10

(B) C-60's
7 departed Miami or W.Palm Beach
3 at Miami
4 at West Palm Beach
1 en route West Palm Beach
15

7. HUDSON III-A
(A) Off L/L Contract AC-4
116 delivered to Debert
4 at Montreal
2 at Ottawa
12 at Montreal for Debert
3 at Detroit for Debert
5 under repair
2 at Long Beach (transition training)
33 for China
20 diverted to U.S. Navy
153 taken by A.A.F.
6 crashed (5 in U.S; 1 in Canada)
356
(61 shipped
417 Total reported away from plant)

(B) Off L/L Contract AC-183
117 delivered to U.K.
22 at Gander
5 en route Gander
10 at Montreal
19 at Detroit
1 en route Detroit
1 at Burbank
4 at Long Beach
6 crashed (3 in U.S; 2 in Canada; 1 en route U.K.)
185
(67 shipped
20 to be shipped
1 crashed (on acceptance flight)
273

U. S. SECRET - BRITISH MOST SECRET

CONFIDENTIAL REPORT | Sheet 3 | MAY 6, 1942
REP. NO. B-65

LOCATIONS OF OCEANIC FLIGHT DELIVERY AIRCRAFT — WEEKLY REPORT NO. [illegible]

8. C-87's off BSC Req. 1050
6 departed Miami
2 at West Palm Beach
8

9. B-17 E's (Army Release) off BSC Req. 1055
7 delivered to U.K. (modified)
1 at Gander (modified)
3 at Montreal (modified)
1 at Detroit (modified)
2 at Wright Field (modified)
7 at Cheyenne (modification center)
12 retaken by A.A.F.
33

10. B-24 D's (Army Release) BSC Req. 1055
7 delivered to U.K. (unmodified)
1 at Gander (unmodified)
1 at Gander (modified)
3 at Montreal (unmodified)
1 at Montreal (modified)
3 at Detroit (unmodified) (for LaGuardia)
6 at LaGuardia Field (modification center)
1 en route modification center
1 crashed (unmodified) (lost en route U.K.)
24

11. B-25 D's (Army Release) BSC Req. 1055
6 at Montreal (modified)
9 at Detroit (modified)
8 at St. Paul (modification center)
23

12. B-25 C's (Army Release) BSC Req. 1055
48 at Kansas City (modification center)
16 at St. Paul (modification center)
29 retaken by A.A.F.
9 en route Kansas City
102

13. B-26 A's (Army Release) BSC Req. 1055
67 at Omaha (modification center)
3 en route modification center
1 crashed (en route modification center)
71

U. S. SECRET - BRITISH MOST SECRET

CONFIDENTIAL REPORT
B.A.C. NO. B-55

Sheet 4

MAY 6, 1942

LOCATIONS OF OCEANIC FLIGHT DELIVERY AIRCRAFT -- WEEKLY REPORT NO. 30

PARAGRAPH:	1	2	3	4	5	6	7	8	9	10	11	12	13	TOTAL
UNITED KINGDOM	58	173	211	8	112		117		7	7				695
MIDDLE EAST	5													5
AUSTRALIA					27									27
SINGAPORE					9									9
Bluie West 1	1													1
In Ferry Service	2													2
Goose				1										1
Gander	1			9			[illegible]		1	2				35
En route Gander				12			5							17
Dartmouth					8									8
Montreal	16	3	4	67	4		26		3	4	6			133
Debert		39					116							155
Ottawa							2							2
Bermuda					3									3
Departed Miami or W.Palm B.						13		6						19
Miami						4								[illegible]
West Palm Beach				5		4		2						11
En route W.Palm Beach						1								1
Detroit	2	1		95			22		1	3	9			133
En route Detroit	1			11			1							13
Burbank							1							[illegible]
Wright Field				1					2					3
To be returned by A.A.F.	3													3
Modification centers									7	6	8	64	67	152
En route mod.centers										1		9	3	13
Long Beach				3			6							9
Under repair		2	1				5							8
For China							33							33
Diverted to U.S. Navy							20							20
A.A.F. Pan. Pro.			19											19
Taken by A.A.F.	44					3	153							200
Retaken by A.A.F.	6								12			29		47
Crashed		7	10	1	2		12			1			1	34
TOTAL	139	225	245	213	165	25	541	8	33	24	23	102	71	1814

Column: 1. Liberator II off Contract F-677
2. Hudson V off Contract A-1749
3. Hudson III off Contract A-68
4. Venturas off Contract A-344
5. Catalinas off Contracts A-2587, F-210, A-37, ADB-58, CAN-76, and BSC Req. 10772
6. Lodestars off L/L Contract AC-53 (BSC Req. 1049)
7. Hudson III-A off L/L Contracts AC-5 and AC-151 (BSC Reqs. 62, 2467, 2718, 3371)
8. C-53's off BSC Req. 1050
9. B-17 E's (Army Release) BSC Req. 10552
10. B-24 D's (Army Release) BSC Req. 10551
11. B-25 B's (Army Release) BSC Req. 10558
12. B-25 C's (Army Release) BSC Req. 10559
13. B-26 A's (Army Release) BSC Req. 10556

U. S. SECRET - BRITISH MOST SECRET

AIRFRAME DIVISION
PLANNING & PRODUCTION DEPARTMENT
BRITISH AIR COMMISSION

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE May 8, 1942

TO Secretary Morgenthau

FROM Mr. White

Subject: British memoranda on their dollar position and on their proposed terms of reciprocal aid.

There are attached several memoranda from the British Government and one from the Australian Government. The first reviews the prospects of Britain's dollar position for the 12 months beginning April 1, and the others state the terms under which the British and Australian Governments wish to extend reciprocal aid.

I. The proposals made in the memoranda may be summarized as follows:

1. There should be no further transfer of capital assets or gold between the United States and the Sterling Area;

2. The United States should take over British airplane contracts;

3. For its part, the British Government would agree that it should not accumulate dollars beyond an adequate working balance. Gold holdings are considered to be outside the working balance, and it is implied that they would continue to increase;

4. The British Government would further agree to provide reciprocal aid from itself and its colonies (not dominions) for all U.K. military and naval exports, for some troop supplies in the Sterling Area, and for some of the costs of the construction and maintenance of bases. An outline of the terms of this reciprocal aid proposal is given on page 3.

5. The Australian Government states that it is generally in agreement with the U.K. memoranda on reciprocal aid, but that the magnitude of the problem is greater in Australia, and it would like to discuss the matter further.

II. The British case for these proposals is as follows:

1. The British have maintained since last February that current gold production must be held as a reserve against their accumulating sterling debt, and that it cannot therefore either be sold to the United States or counted amongst their available dollar assets. The memoranda state that their sterling debt is accumulating at a rate of $2 billion annually, and that the United Kingdom will not receive more than $500 million annually from the current gold production of the Empire.

Division of Monetary
Research

2. Excluding gold production, the British memoranda state that they will have a dollar deficit on current account of $250-$300 million in the 12 months beginning April 1, 1942. To this deficit must be added approximately $450 million of payments due on B.P.M. contracts, making the total deficit $700-$750 million. (These estimates agree approximately with our estimates. See page 4 for our estimates.) To offset this deficit the British anticipate approximately $390 million of special receipts. A list of the special receipts and our comments upon them is given on page 5. Because the special receipts are inadequate to meet the expected deficit, and the British Government requests that their airplane contracts, amounting in all to about $450 million, be taken over.

III. Comments on the British proposals:

1. Expected British receipts for the coming 12 months are inadequate to meet their current expenditures and payments on remaining B.P.M. contracts only if we accept the British contention that receipts from current gold production should not be counted amongst their dollar receipts and dollar assets. Hence, their case for the take-over of airplane contracts depends upon acceptance of their case for earmarking current gold production against sterling debts. If gold production is included in their dollar receipts and assets, British gold and dollar holdings, which were $615 million on April 1, would total $755-805 million on April 1, 1943, without the take-over of airplane contracts. If, in addition to this, their $450 million of airplane contracts were taken over, their gold and dollar balances would amount to $1,205-$1,255 million by next April, or twice as much as the United States Treasury has considered to be adequate.

2. The British proposals for reciprocal aid appear to be satisfactory, but they should not be made to depend upon our acceptance of the other proposals.

Terms suggested by the British for Reciprocal Aid from the United Kingdom and its Colonies.

A. Types of transaction

(1) Exports to U.S.

(a)	commercial and raw material exports	U.S. pay dollars
(b)	U.K. military and naval exports	Reciprocal aid to either U.S. or its authorized contractors. (profit limitation imposed.)
(c)	Items from Britain's dollar contracts	U.S. pay dollars.

(2) Expenses for U.S. Troops in Sterling Area

(a)	pay and allowances	U.S. purchase local currency with dollars.
(b)	troop supplies	Either reciprocal aid or U.S. purchase or importation, depending upon convenience. U.K. would refund any payments made for materials previously imported under Lend-Lease,
(c)	oil	Special case. Reciprocal aid unless it cost U.K. dollars.
(d)	construction and maintenance of bases	Government making the base to bear the cost with no apportionment of expense on the basis of use, and with no lend-lease or reciprocal aid obligation. U.K. would like this to be "retrospective" (retro-active?). However, all dollar costs would be met by U.S. or provided on Lend-Lease, and U.K. would provide supplies and services for projects in U.K. or colonies.

Estimated U. S. dollar expenditures and receipts of the Sterling Area on current account April, 1942 to April, 1943

Dollar Expenditures

	(In millions)	
A. Payments to U. S. by U. K.		
1. On British Purchasing Mission commitments	$450	
2. For other merchandise imports outside Lend-Lease	120	
3. For services	105	
4. All other	80	$755
B. Payments to U. S. by other sterling area		
1. For merchandise imports	$170	
2. For services	70	240
C. Payments by sterling area outside U. S. requiring gold or dollars		
1. For oil	$ 60	
2. All other payments including 40 million of payments to Iran	85	145
Total estimated United States dollar expenditures		$1,140

Dollar Receipts

A. Receipts from U. S. by U. K.		
1. For merchandise exports	$100	
2. For services	70	
3. All other	80	$250
B. Receipts from U. S. by rest of sterling area		
1. For merchandise exports	$160	
2. For services	40	200
Total estimated United States dollar receipts		$450
Estimated dollar deficit of sterling area on current account April, 1942 - April, 1943		$690 *

* **This deficit of $690 million compares with the deficit stated in the British memoranda of $700 - 750 million.**

Treasury Department, Division of Monetary Research May 8, 1943

The British anticipate the following special receipts during the year beginning April 1942

Balance of R.F.C. loan 1/) Wool sales)	$40
Sale of capital facilities 2/	90
Payment already received for airplanes diverted to U.S.	70
Additional payment for airplanes diverted to U.S. or Russia	?
Take-over of ordnance contracts 3/	90
Dollar receipts from U.S. troops in Sterling Area 4/	100
Total, at least	$390

1/ The balance due on the R.F.C. loan is $35 million, but the R.F.C. may not be willing to extend more than $25 million.

2/ This figure envisages the sale of all British armament plant facilities.

3/ Our figures indicate the British will not be able to obtain more than $70 million from this source unless the War Department is willing to refund some portion of the advance payments made on ordnance contracts.

4/ This figure is much lower than our estimate of the sterling area receipts from American troops. Our figure for military pay alone in calendar year 1942 is $202 million, and it would unquestionably be larger for the 12 months beginning April 1942. The figure for civilian pay, some of which will be paid in dollars is $412 million for calendar year 1942.

338
Aid to Br.

May 4, 1942

Mr. White

Mr. Hicks

Subject: Sir Frederick's Memorandum on Britain's Dollar Position

1. A dollar deficit on current account (i.e. excluding gold production, capital sales, and payments on B.P.M. contracts) of $250 - 300 million is predicted for the 12 months beginning April 1, 1942. Including B.P.M. payments, the deficit will be $700 - $750 million.

2. These estimates agree reasonably well with our own estimates for similarly defined categories.

3. The British anticipate the following special receipts:

(a)	balance of R.F.C. loan 1/ }	$40
(b)	wool sales }	
(c)	sale of capital facilities 2/	90
(d)	payment already received for airplanes diverted to U.S.	70
(e)	additional payment for airplanes diverted to U.S. or Russia	?
(f)	take-over of ordnance contracts 3/	90
(g)	dollar receipts from U.S. troops in Sterling Area 4/	100
	Total, at least	$ 390

4. If current gold production of $500 million, as estimated by the British, is added to these special receipts, the total of $890 million would be larger than the expected deficit of $700 - $750 million, and British gold and dollar holdings would increase from the $615 million (the British have included "scattered gold" and "gold held against immediate liabilities" in this figure) held on April 1, 1942 to $755 - $805 million on April 1, 1943. This total would be reached without any further sale of American securities. 5/

5. However, the British memorandum repeats the contention advanced since February that current gold production must be held as a reserve against their accumulating sterling debt, and requests acceptance of the following program:

(a) U.K. be required to make no further sales of gold or capital assets;

(b) U.S. take-over British aircraft contracts in the United States.

Division of Monetary Research

The value of undelivered aircraft materials is $450 million, and if these were taken over the British gold and dollar balance including new gold production would be $1,205 - $1,255 next April, or twice as large as the amount the U.S. Treasury has considered to be adequate.

6. A problem exists, therefore, only if we approve the British contention that current gold production should be earmarked as a specific reserve against their accumulating sterling debt. The British memorandum states that their sterling debt is accumulating at a rate of $2 billion annually. This contention raises a number of problems:

(a) The British have advanced this contention repeatedly since last February. I do not believe that we have ever accepted or denied it. If it is not denied it may be assumed to have been tacitly accepted.

(b) Sir Frederick justifies the contention on the ground that the sterling debt "will have to be repaid some day." It is clearly implied that sterling obligations - even those held by the Empire - are a prior claim to British income.

1/ The balance due on the R.F.C. loan is $35 million, but the R.F.C. may not be willing to extend more than $25 million.

2/ This figure envisages the sale of all British armament plant facilities.

3/ Our figures indicate the British will not be able to obtain more than $70 million from this source unless the War Department is willing to refund some portion of the advance payments made on ordnance contracts.

4/ This figure is much lower than our estimate of the sterling area receipts from American troops. Our figures for military pay alone in calendar year 1942 is $202 million, and it would unquestionably be larger for the 12 months beginning April 1942. The figure for civilian pay, some of which will be paid in dollars is $412 million for calendar year 1942.

5/ Marketable securities available for sale amount to about $65 million.

JBH/grs - 5/4/42

MEMORANDUM

1. British holdings of gold and dollars (excluding the Belgian loan) rose from about $190 millions on March 31, 1941 to $615 millions a year later. The increase in the year ended March 31, 1942, thus amounted to $425 millions. During the year the position of the United Kingdom worsened by about $3 billions, of which nearly $2 billions represented the growth of overseas balances in London, which will have to be repaid some day.

An approximate analysis of the increase in the balance during the year is shown by the following figures:

		$ Millions
Gold, net acquisition *		505
Special receipts:		
from RFC loan	390	
from direct investments (Viscose and B.A.T.)	80	
from market securities	90	
from South African securities (special sale for gold)	130	
from sale of wool stock	40	730
Net credit on current $ account		90
		1,325
less Net payments on British Government contracts in the U.S. **		900
		425

* Excluding special purchase of gold from South Africa shown under capital receipts. The acquisitions of newly-mined gold from South and other Africa was $455 millions, Australasian gold (mainly sold direct to U.S. before Pearl Harbor) was about $60 millions, other acquisitions of gold (from dishoarding, Russia, etc.) was $60 millions. Of the total of $575 millions, $70 millions was sold direct to countries other than U.S., giving a net acquisition of $505 millions. Sales to U.S. (including direct Australian sales) amounted to approximately $100 millions, included in the figure of $505 millions.

**Deducting sales of capital facilities (e.g. Tennessee Powder) and refunds on contracts taken out by the United States.

2. It may be noted that if there had been no old contracts to pay for, and no special receipts, the year would have shown a small gain of $90 millions, apart from newly-mined gold. Had this state of affairs continued for the rest of the war, the newly-mined gold would have accumulated as a small but useful reserve against the liabilities represented by the growth of overseas sterling balances. But the sterling area, since the entry of the United States into the war, no longer brings us in a favourable balance of dollars.

The loss of Malayan exports alone amounts to $300 millions a year. There is a large but as yet unknown fall to be faced in Indian and Burmese exports. Meanwhile, United Kingdom exports, not only to the United States but to all destinations, are steadily falling owing to lack of shipping, labour and raw materials. Instead of a small net gain, there will be a large current deficit in the coming year which might amount to as much as $250 - $300 millions.

British Government contracts still outstanding in the United States on the 1st April last required payments of about $430 millions before they run out early next year. Taking account of rising costs (not fully allowed for in this figure) and of administrative expenses, we have at least $450 millions to pay during the year.

The sterling area may, thus, need to find dollars to an amount of $700 to $750 millions during the coming year, with a continuing though smaller deficit thereafter.

3. The liabilities of the United Kingdom to sterling area and other countries outside the United States are already very large and the present British gold holding is but a small reserve against them. We had been at war more than two years before December 7th last and had been fighting the United Nations' cause practically alone for over 18 months. For a considerable time more than half of the national income

of the United Kingdom has been spent on the war. But, as a result of the burden carried so long alone, British investments in the United States have been largely sold or pledged while British indebtedness to India, South Africa, South America and other countries has grown to large proportions.

The present British gold holding must, therefore, be maintained against liabilities outside the United States.

4. This is, however, not the end of the story. Additional liabilities to countries other than the United States are being incurred on an increasing scale. It is estimated that additional liabilities during the coming year will amount to £500 millions, or $2,000 millions, even when we allow for the Canadians' generous gift. The net acquisition of gold will almost certainly fall short of the amount received in the past year, especially if mining equipment is not forthcoming from the United States in sufficient quantities to maintain output and since some sources (e.g. New Guinea) have been cut off and others threatened by the war. We can count on less than $500 millions a year, i.e., less than one-quarter of the additional liabilities we expect to incur. The British Government is, therefore, most concerned that the current gold output should be retained as a partial reserve against currently incurred liabilities.

5. In the circumstances described the British Government asks that arrangements should be made which will make it unnecessary for any further gold or other capital assets (other than capital facilities mentioned above) to be sold to the United States. In this event how is the dollar deficit of $700 to $750 millions to be found in the coming year ?

Special receipts will comprise only the balance of the RFC loan and a little to come from special wool sales, say $40 millions altogether. No further special purchase of South African gold, other than of the output of newly-mined gold is possible. Sale of capital facilities might come to $90 millions (of which $60 millions for the eleven cases covered by the President's directive, and $30 millions for new cases). For airplanes handed over after Pearl Harbour we have received $70 millions; the balance to come is not yet known. This reduces the figure to $500 millions - $550 millions.

6. The most appropriate method for enabling us to meet this expected deficit is a bulk take-out of our remaining dollar contracts. Planes and munitions supplied from our pre-lend-lease contracts are now regarded as being at the disposal of combined boards and are allocated by these boards in accordance with strategic needs. The move towards a pool of overseas resources is further emphasised by the reciprocal lend-lease proposals. The United States Government has already agreed to take over our outstanding ordnance contracts and we should hope to obtain assistance by this means of some $90 millions. It will be seen that if the estimate in this memorandum is correct, this is far from enough. The value of the deliveries still to be made under our air contracts is about $450 millions, $250 millions of this represents payments still to be made under the contracts and the remaining $200 millions represents payments made in advance. Both because of the pooling of supplies and because of our need of additional reserve we ask that the air contracts as well as the ordnance contracts should now be taken over.

7. As indicated above there may be further receipts in respect of airplanes, etc., taken over after Pearl Harbour or for Russia and China. Moreover, the presence of United States troops in the sterling area will produce some dollars. But the latter will hardly exceed $200 a man a year, and this source of dollars would only reach $100 millions on the basis of 500,000 men in the sterling area on the average throughout

the year. The effect of reverse lend-lease itself, which the United Kingdom hope to make as generous as possible, is somewhat adverse to our dollar position.

The principle we seek to establish is that there should be no further transfer of capital assets or gold, and that we should not attempt to build up anything beyond a working balance in dollars.

Willard Hotel,

Washington, D.C.,

May 2, 1942.

O 3453

April 30, 1942

The Secretary

Mr. White

Subject: Outline of Attached British Memoranda on Reciprocal Aid

I. Introductory Memorandum:

A. U.K. desires to extend reciprocal aid, but is limited by its finances, overseas obligations, the loss of Empire exports, and the "increasingly inappropriate" financial arrangements with U.S., particularly the continuation of payments on dollar contracts for materials destined for a common pool.

B. H.M.G. suggests as a principle

(1) "No further transfer of capital assets or gold between U.S. and Sterling Area." Apparently this provision would preclude further sale of British securities.

(2) The Sterling Area "should not accumulate dollars beyond an adequate working balance." It is implied that gold holdings are outside the working balance and that they would continue to increase.

(3) U.K. could then provide reciprocal aid from itself and its colonies (not Dominions) according to the following plan:

II. Memorandum on Reciprocal Aid from U.K. and its Colonies:

A. Types of transaction

(1) Exports to U.S.

(a) commercial and raw material exports	U.S. pay dollars.
(b) U.K. military and naval exports	Reciprocal aid to either U.S. or its authorized contractors. (profit limitation imposed.)
(c) Items from Britain's dollar contracts	U.S. pay dollars.

(2) Expenses for U.S. Troops in Sterling Area

(a) pay and allowances	U.S. purchase local currency with dollars.
(b) troop supplies	Either reciprocal aid or U.S. purchase or importation, depending upon convenience. U.K. would refund any payments made for materials previously imported under Lend-Lease.
(c) oil	Special case. Reciprocal aid unless it cost U.K. dollars.

1 Or. to Miss Chauncey with or. of attachment; cc of memo to D.W. Bell and photostat of attachment

(4) construction and maintenance of bases	Government making the base to bear the cost with no apportionment of expense on the basis of use, and with no lend-lease or reciprocal aid obligation. U.K. would like this to be "retrospective" (retroactive?). However all dollar costs would be met by U.S. or provided on Lend-Lease, and U.K. would provide supplies and services for projects in U.K. or colonies.

B. Procedure

(1) Requisitions for reciprocal aid to be filed in London.
(2) U.K. cannot keep full records and suggests that no records be kept of such services as repairs.
(3) Shipping arrangements need further discussion.

III. Australian Memorandum.

A. Australia is generally in agreement with U.K. memoranda, but suggests that the magnitude of the problem is greater in Australia, and requests that the matter be discussed further.

HEH:gs - 5/1/42

MEMORANDUM

His Majesty's Government are anxious to grant reciprocal Lend-Lease aid to the United States of America on the most generous scale possible, and are well aware of the political importance attaching to the matter, but the extent of the assistance which they can give is necessarily affected by their financial position. The United Kingdom is already defraying war expenditure equal to sixty percent of the national income and the rates of taxation in force are the heaviest of any of the United Nations.

Progress towards a financial settlement is now urgent and H.M.G. submit that the present financial arrangements are increasingly inappropriate. Munitions supplied from our pre-lend-lease contracts are now regarded as being at the disposal of Combined Boards and are allocated by these Boards in accordance with strategic needs. The move towards a pool of overseas resources is further emphasized by the reciprocal lend-lease proposals, the principle behind which we accept and warmly approve.

It seems quite inappropriate in present circumstances that we should be required to ship to the United States currently mined gold, which can surely be of little value as an addition to United States resources, to pay for munitions which will be as much at the disposal of the United States as at ours. We can only obtain such gold by increasing our overseas indebtedness and even if we had no payments to make in the United States or Canada and were acquiring no gold, we should still have to increase our overseas indebtedness by upwards of £400 millions to meet our growing expenses elsewhere. This point is frequently overlooked. It is not merely that we export less and import much more from the United States and Canada. The same thing happens with every other country from which we draw supplies.

The annual increase in the liabilities now being incurred by the United Kingdom to countries other than the U.S.A. and Canada, is not less than four times the total amount of the present output of gold by the sterling area, and H.M.G. are anxious that the gold output should be retained as a partial reserve against these liabilities. At the same time the possibility of holding or accumulating a reserve has been heavily reduced by the loss of tin and rubber exports, by the loss of exports, which it is impossible yet to estimate, from India, and the absence or shortage of shipping, labour and raw materials resources in the United Kingdom itself.

H.M.G. suggest as a general principle that from now on there should be no transfer of capital assets or of gold between the United States and the sterling area, and that at the same time the sterling area should not accumulate dollars over and above an adequate working balance. If this is to be done a new settlement involving the remaining pre-lend-lease contracts is urgently required.

If arrangements can be made to carry this general principle into effect, H.M.G. would hope not only to extend reciprocal lend-lease aid on the desired scale, but also to avoid difficulties and possible criticism arising out of the bringing of borderline or doubtful cases within the ambit of the lend-lease system.

(Sgd.) F. Phillips

Washington, D.C.,

April 18, 1942.

FP:KF

MEMORANDUM

1. MILITARY STORES

We propose to supply munitions, military and naval stores (not including local supplies for United States forces abroad for which see below) and associated services on Lend-Lease terms to the United States Government. These supplies if requested from and furnished through a recognized Government organisation would be made on lend-lease terms whether they are issues from stores or whether they involve the placing of special contracts by the supplying Government. They would similarly be made available to contractors working for the United States Government on specific request of the United States Government to that effect, and on the assurance that the contractor is acting on behalf of the United States Government and that steps will be taken to prevent his making an uncovenanted profit.

The above offer would not apply to commercial supplies or to raw materials except that minor supplies of raw materials might be more properly dealt with as military stores and furnished on Lend-Lease terms at the discretion of the supplying Government.

Munitions, etc., off United Kingdom dollar contracts would not be transferred under reverse lend-lease, but should be paid for in dollars. We should not, however, claim dollars for materials which had already entered our depots except when they can be distinguished from lend-lease or sterling materials.

2. UNITED STATES FORCES IN STERLING AREA

United States would purchase the local currency required for pay and allowances and for local cash disbursements.

As regards supplies other than munitions and strictly military stores for American forces in the sterling area, it is not possible owing to the variety of considerations which may arise, to lay down precise rules in advance. It would have to be settled on considerations of convenience from the point of view of supply, shipping and administration whether particular supplies should be made available on reverse lend-lease by local purchase or by importation by the United States Government.

As regards American forces in the United Kingdom, the arrangements would be settled in London between the Service Departments and the United States Missions who are in daily contact on these matters, and broadly speaking, the supplies such as food, fuel, etc., are being treated on the same lines as munitions.

Arrangements would have to be made to avoid possible criticism if United States Purchasing Officers paid for particular goods previously received by the United Kingdom under Lend-Lease. This would be done by refunding in any particular cases claimed by the United States authorities. If desired a short list of important articles could be agreed on which a general refund would be made of a proportion of the cost corresponding to the proportion of Lend-Lease supplies to the total supplies in the United Kingdom.

Oil is a special case. Broadly speaking, H.M.G. would provide both lend-lease and sterling oil on reverse lend-lease, but would expect to be recouped any dollar expenditure in the case of oil supplies (e.g., from Bahrein) which had involved the United Kingdom Government in such expenditure.

3. <u>TASKS AND OTHER CAPITAL WORKS</u>

The original conception of tasks and other capital works as works carried out on our behalf by the United States should, since the entry of the United States into the war, be revised to a conception of them as joint works carriedout for the mutual benenfit of the two countries. It is suggested that:-

(i) The initial cost should lie where it falls; i.e., the government responsible for construction, maintenance, and/or operation should bear the cost, including the provision of local currency, except for such supplies and services as it may be convenient for other governments to contribute. Dollar costs would, in all cases, be provided on Lend-Lease. We should be willing to make available supplies and services for tasks being carried out by the United States Government in United Kingdom and the Colonial Empire. In the Middle East, whichever government has assumed responsibility as above should normally itself obtain supplies and services by local purchase wherever expenditure in local currency is involved.

(ii) The contribution by each government to the capital and running costs should finally dispose of the question of the respective liability of the two countries and no attempt should be made on either side to record lend-lease or reverse lend-lease liabilities or to apportion the liability according to user benefit. This disappearance of book records and apportionment's right, it is suggested, be made retrospective.

H.M.G. would like the above principle of no account and no liability in connection with works of mutual benefit extended as widely as possible.

4. PROCEDURE

United States demands for reverse lend-lease should be presented not to the Missions in Washington, but to the appropriate department in London by the appropriate United States Mission.

In the case of assignable stores the appropriate department would keep the London Munitions Assignment Board informed, and its decisions would be communicated to the Combined Munitions Assignment Committee in Washington. It is important that the American requests should follow the above channel and not be presented direct to the suppliers.

5. DOMINIONS AND COLONIES

We will take the responsibility as regards the Colonies and the same principles will be applied as in the United Kingdom.

As regards the Dominions and India they have been, and will be, kept informed of our views. So far as possible uniform criteria for reverse lend-lease will be applied, but there will no doubt be difference of detail between the various Dominions.

6. RECORDS

We cannot keep complete priced records, and there can be no joint accounts or records. We must ask the United States not to expect full records from us. No standardised requisiton form is suggested for reverse lend-lease. In particular no records are being kept of services (e.g. repairs of army trucks) rendered by British to United States forces. In view of the fact that records of such services must in any case be extremely incomplete we suggest that it is important that the principle should be followed that no record should be kept on either side in the case of miscellaneous services.

7. SHIPPING

Under the head of shipping, questions of reverse lend-lease depend rather intimately on the arrangements made as regards direct lend-lease, and in view of the complications and technicalities involved, the matter needs direct discussion between the War Shipping Administration and the British Shipping Mission.

(Sgd.) F. Phillips

Willard Hotel

Washington, D.C.

Ap[illegible] 24, 194[illegible]

C
O
P
Y

RECIPROCAL LEND LEASE.

1. Australia is supplying war stores to United States forces in Australia, and has provided supplies for United States forces in the Philippines to the value of about £500,000. It has also approved the construction of special defence works in Australia to a value of about £5,000,000 in excess of the requirements of its own forces, and is considering a much larger programme of the same kind, estimated at present to cost about £50,000,000 and required by the United States forces.

2. Australia desires to come to an arrangement with the United States on these matters, and to enter into joint discussion on aspects of mutual interest with representatives of the United States and of the United Kingdom, with a view to a common understanding on the principles to be followed based on the terms of the Mutual Aid Agreement of Feb. 23rd between the United States and the United Kingdom, and on views which have been expressed by the Department of State.

3. A memo of current date setting out the proposals of the United Kingdom in connection with similar arrangements, has been noted. The Australian view is generally in accord with the suggestions made therein, but it is desired to state certain special Australian considerations which have been communicated by the Prime Minister.

4. The magnitude of Australian supplies to the United States forces is likely to be proportionately greater than those of the United Kingdom or of any other country, with respect to -

(a) the range of supplies, and
(b) the population and resources of the country, e.g.

(i) The range of stores to be supplied will include prepared foods and personal equipment for the forces, which in other theatres will normally be provided from the United States. It may also include a larger proportion of arms and ammunition and other military stores and maintenance than could be provided locally to U.S. forces in other countries.

(ii) The supply of all such stores to United States forces in the South-Western Pacific areas other than Australia may become large also, particularly when a strong offensive is launched with Australia as a base.

(iii) The Works proposed are much in excess of the needs of Australia, other than as a base for United Nations operations. The addition of these "Tasks" to an already crowded programme will strain the resources of the country and reduce production for commercial export, with consequential reductions in overseas funds.

5. Australia is a debtor country with large annual liabilities for interest etc. It also has very heavy liabilities in sterling, and in U.S.A. and Canadian dollars, for special war expenditures both with respect -

(a) to the maintenance of its forces in various theatres of war, or
(b) to the purchase of war equipment and components in the United States, Canada and the United Kingdom.

Despite certain countervailing credits, which cannot be discussed, and severe restrictions on civil imports from all sources, Australia is at present faced with a heavy deficit on overseas account.

6. It is the desire of the Australian Government to contribute what is needed in and from Australia to the fullest possible extent, but its circumstances are difficult and peculiar to itself. It is realised that these facts are appreciated both by the United States and the United Kingdom, and it is hoped that a solution satisfactory to all concerned will emerge from the proposed discussions.

May 6, 1942

Mr. Livesey

Mr. Dietrich

Please send the attached cable to the American Embassy, London; "For Casaday from the Secretary of the Treasury".

FD:lo:5/6/42

TO E.G. Casaday,
American Embassy,
London, England.

FROM The Secretary of the Treasury

Please cable at once whatever information you can obtain quickly in answer to the following questions:

(1) In connection with present British individual income taxes, have any provisions been made to relieve taxpayers with relatively large contractual obligations such as life insurance, long-term leases and mortgages and other debt repayments? Presumably increased income taxation has made it difficult for some persons to meet such contractual obligations.

(2) What has been the effect of the increased rates on the living standards of the upper income classes? It has been suggested that living standards have been retained and supported from liquidation of assets despite the virtual limit on the amount of current income remaining after tax.

(3) Is there evidence that evasion or avoidance has been attempted or that any important loopholes have developed to reduce the effectiveness of the tax rates?

(4) Is there evidence that high rates have reduced appreciably the incentive in the upper income groups to continue in gainful occupation?

RBM:gp 6/7/42

TELEGRAM SENT

HRL PLAIN

May 8, 1942

AMEMBASSY

LONDON (ENGLAND).

2010, eighth.

For Cassaday from the Secretary of the Treasury.

QUOTE. Please cable at once whatever information you can obtain quickly in answer to the following questions:

(1) In connection with present British individual income taxes, have any provisions been made to relieve taxpayers with relatively large contractual obligations such as life insurance, long-term leases and mortgages and other debt repayments? Presumably increased income taxation has made it difficult for some persons to meet such contractual obligations.

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developed

-2- #2010, May 8, 1942 to London, England.

developed to reduce the effectiveness of the tax rates?

(4) Is there evidence that high rates have reduced appreciably the incentive in the upper income groups to continue in gainful occupation?

HULL
(FL)

FD:FL:BMcB

COPY

EMBASSY OF THE
UNION OF SOVIET SOCIALIST REPUBLICS
WASHINGTON, D. C.

May 8, 1942

My dear Mr. Secretary:

I wish to acknowledge the receipt of your letter of May 7 informing me of the allocation of the net value of the gold deposit of $11,222,110.13.

I am cabling this information to the Soviet State Bank.

Yours sincerely,

(Signed) Maxim Litvinoff

Ambassador

The Honorable
The Secretary of the Treasury
Washington, D. C.

COPY:lap-5/9/42

MAY 8 1942

My dear Mr. Secretary:

Reference is made to your letter of March 27, 1942 (TA), enclosing copies of a draft text of the general provisions, Final Minutes, related notes and Schedule II of the proposed trade agreement between the United States and Uruguay.

Reference is also made to the letter addressed by the Chief of the Division of Commercial Policy and Agreements of the Department of State to the Director of Monetary Research of this Department on April 30, 1942, relative to the scope of Article X of the proposed agreement.

An examination of the submitted provisions of the proposed trade agreement, when considered in the light of the letter of the Chief of the Division of Commercial Policy and Agreements referred to above, discloses no administrative difficulty for the Treasury Department which would warrant objection by me to the conclusion of the agreement.

Very truly yours,

(Signed) H. Morgenthau, Jr.

Secretary of the Treasury.

The Honorable,

The Secretary of State.

BCthl 5-4-42

File to Thompson
cc - N.M.C.
By messenger Sturgis 4:40

COPY NO. 13

BRITISH MOST SECRET

(U.S. SECRET)

OPTEL No. 152

Information received up to 7 A.M., 8th May, 1942.

1. MADAGASCAR

French Forces on the ORONJIA Peninsula (south of DIEGO SUAREZ BAY and east of ANTSIRANE) have surrendered. The Fleet has entered DIEGO SUAREZ Harbour. During sixth, two enemy bombers were certainly and one probably destroyed by our fighters.

2. NAVAL

One of H.M. motor launches has been sunk by enemy action off MALTA. One small Russian ship sunk off NORTH CAPE on first.

3. AIR OPERATIONS

WESTERN FRONT. 6th/7th. About 80 tons of high explosives and incendiaries dropped on STUTTGART area, extensive fires reported.

7th. Twelve Bostons attacked coke ovens at ZEEBRUGGE, which was seen to be enveloped in smoke, and power station at OSTEND. 21 Squadrons of Spitfires provided escort and carried out one sweep, but no conclusive combats took place. A Junkers 88 was destroyed south of PORTLAND.

7th/8th. Aircraft were despatched - Sea mining 81 (east coast DENMARK and HELIGOLAND), ST. NAZAIRE 5, Leaflets Vichy 1. Two aircraft are missing. A convoy of 12 ships was attacked off TEXEL. Preliminary reports indicate that about ten hits were obtained. Two Hudsons are overdue. A small number of enemy aircraft operated over this country, causing slight damage in KENT and SUSSEX. Two were destroyed by Beaufighters.

EGYPT. 3rd/4th. 20 enemy aircraft bombed ALEXANDRIA causing slight damage. Beaufighters destroyed one and damaged two, whilst anti-aircraft probably destroyed another.

BURMA. 5th. Blenheims made a successful low-level attack on loaded barges at MONWA several being hit.

5th/6th. Wellingtons, bombed AKYAB. Three Fortresses started large fires at MINGALADON aerodrome.

4. INTELLIGENCE

French Navy. There was no change in the disposition of French Naval Units at DAKAR on 6th May.