GERMANY'S EXTERNAL ECONOMIC POSITION

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The monetary reform of mid-1948, which in introducing the Deutsche mark (D-mark) canceled approximately 90 per cent of Germany's cash holdings and deposits, awakened her economy from the stagnation into which it had fallen after the surrender. Black-market and barter transactions which, along with trading at fixed prices under rationing and allocation controls, had characterized Germany's exchange economy in the early postwar years, disappeared overnight; and a homogeneous price system re-emerged. Most important, the cancellation of a large proportion of the monetary "overhang," that was a legacy of the war, created incentives to work and to save. Production, which prior to the reform had been running at very low levels, made spectacular advances. In short, the reform brought about what has become known as the "miracle of the D-mark."

This miracle, however, could not have been performed, and could not have had more than passing effects, without strong initial injections of United States aid and the adoption by Germany of well-considered economic and fiscal policies. First, most of the wartime controls, such as price controls and rationing, which had been continued under the occupation, were abolished with a view to restoring a high degree of *laissez faire*. Secondly, the tax system was overhauled so as to encourage investments and exports rather than consumption. Thirdly, orthodox monetary policies have been followed, which, especially at the time of the Korean boom, helped to keep inflationary pressures from exerting undue influence on the wage and price level and on Germany's ability to compete in world markets.

The success of these policies is reflected in Germany's remarkable economic and financial recovery. Her industrial production has increased by more than 140 per cent since 1948; owing mainly to the absorption of laborers from East Germany, the number of employed has risen to 15.7 million in 1953 from 13.5 million in 1949, while the number of unemployed has remained little changed (about 1.2 million), representing, in 1953, 7.8 per cent of the potential labor force. The cost

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of living has remained virtually unchanged since 1949, while real industrial wages have risen substantially.

I. *Balance-of-Payments Developments*

Most striking in the years since the currency reform of mid-1948 has been the general improvement in Germany's balance of payments. From a balance-of-payments deficit on current account the equivalent of more than $1 billion in 1949, Germany worked up to a surplus of more than $900 million in 1953; if the latter surplus is compared with the 1949 deficit, the over-all improvement in Germany's current account position appears to be in the order of magnitude of almost $2 billion. These developments have been reflected in a considerable strengthening in Germany's gold and foreign exchange reserves, which, measured by foreign exchange requirements for imports, are now comparable to those of the sterling area. In addition, the rate for the D-mark in international markets has strengthened considerably; in the multilateral exchange trading instituted in mid-May 1953 between (now) nine European currencies, the D-mark has proved consistently strong; moreover, the very substantial discounts on D-mark notes and on blocked mark balances have virtually disappeared. In line with this progress, German economic and financial policy is at present officially oriented toward restoring a large measure of convertibility to the D-mark.

The primary factor in the striking upswing in Germany's current account position is to be sought in the improvement in her terms of trade. Comparing the first five months of 1954 with the corresponding period in 1950, the volume of exports rose by 167 per cent, and equally important, export prices rose by 19 per cent. Import volume, on the other hand, rose much less, 74 per cent; moreover, except for the year 1951, the rise in import prices was considerably smaller than in export prices, and in the first five months of 1954 import prices were only about 3 per cent above the 1950 level. Consequently, Germany's terms of trade have improved by more than 15 per cent since 1950. The improvement in the terms of trade, combined with a much larger rise in export volume than in import volume, must be considered the principal factor in the over-all improvement in Germany's balance-of-payments position (Table I).

The conspicuous increase in Germany's volume of exports in the early years after the currency reform reflected German ability to bring idle labor and unutilized resources back to work. Over the period as a whole, the relatively high level of business activity in the United States engendered a large demand for imports from Germany in the United States, and indirectly, as a result of rising business activity, in nondollar area countries, thus creating a sellers' market for such Ger-

TABLE I.—GERMAN FOREIGN TRADE VOLUME, AND IMPORT AND EXPORT PRICES

(1950=100)

Year or Quarter	Physical Volume		Average Prices		Terms of Trade[a]
	Imports	Exports	Imports	Exports	
1950	100	100	100	100	100
1951	102	143	127	122	96
1952	118	154	121	131	107
1953	133	180	106	123	116
1950—I	91	72	97	100	103
II	80	85	98	100	102
III	102	105	98	99	101
IV	127	137	107	101	94
1951—I	113	130	116	110	95
II	87	143	130	119	92
III	103	152	136	127	93
IV	105	149	128	129	101
1952—I	115	144	132	131	100
II	99	148	127	133	105
III	112	155	116	132	114
IV	145	171	111	128	115
1953—I	121	151	111	126	114
II	126	174	107	123	115
III	131	180	104	122	117
IV	155	216	98	121	123
1954—I	144	197	100	120	120
II[b]	158	210	100	119	119

[a] Ratio of export prices to import prices: $\frac{\text{(Index of export prices} \times 100)}{\text{(Index of import prices)}}$.

[b] April and May only.

Source: *Der Aussenhandel der Bundesrepublik Deutschland.* Teil I, *Zusamenfassende Übersichten,* Statistisches Bundesamt, Weisbaden, May 1954, and earlier issues.

man products as machinery, cars, and other highly specialized finished products. Germany was therefore able to raise export prices and at the same time increase the export volume. Moreover, as a result of persisting dollar shortages, European nations and nations overseas continued to discriminate against imports from the dollar area and to look for substitute sources of supply. Germany, especially as an exporter of capital equipment, offered an alternative source of supply, and greatly benefited from these shifts in trade. This factor was of considerable importance after Korea when Germany's foreign trade partners started rearming. Unlike her neighbors, she has not had to devote any of her

Germany's exports, moreover, have been encouraged by tax incentives, a system of export credit insurance, and, to a minor extent, long-term export credits and foreign-exchange retention schemes. Aggressive export promotion on the part of private industry through participation in international fairs and otherwise, as well as the fact that German industry is export-minded and flexible in adjusting itself to changing foreign import requirements, may also have played a major part in the country's comeback in international markets.

As regards the development of import prices, Germany has benefited from the decline in primary commodity prices (under way rather steadily since August 1951) more than some of the other European nations. The country appears to have made most of this development by freeing imports from quota restrictions (after her post-Korea balance-of-payments crisis had been overcome) at a more rapid pace than some of the other European nations, thus allowing her importers to buy in comparatively cheap markets. The fact that Germany's terms of trade improved more strongly than those of other nations (see Table II) appears to have been due not only to the relative rise in her

TABLE II.—IMPROVEMENT IN THE TERMS OF TRADE OF SELECTED COUNTRIES
(1950 = 100)

Country	1951	1952	1953
Germany	96	107	116
France	91	102	106
United Kingdom	88	95	104
Netherlands	97	98	99
Belgium-Luxembourg	110	114	102
Sweden	122	115	111

Source: OEEC computations.

resources to the support of an army of her own, and has been free of the economic and defense commitments toward overseas areas that have proved a considerable drain on the economies of several other European nations.

Generally speaking, Germany has been in a favorable competitive position as a result of a relatively low pattern of wage costs, and by following prudent monetary policies which have contributed to keeping the price level from getting out of hand. For various reasons, some of her trading partners both in Europe and overseas, on the other hand, did not follow such policies, with the result that their currencies became overvalued; this condition, in turn, created on their part a higher propensity to import from Germany, while discouraging exports to her.

export prices[1] but also to this favorable set of circumstances on the import side.

The most potent factor in bringing about Germany's favorable balance-of-payments position has been her comparatively low prospensity to import, compared both with the prewar years and with other industrial nations.[2] It appears that, as a result of decades of tariff protection and especially the autarchy movement during the Hitler period, Germany's economy has become relatively self-sufficient. The production and domestic use of newly developed materials as well as the more sparing use of materials in general, whether domestically produced or imported and whether for manufacturing goods for the home market or for export, are characteristic of this development. Moreover, Germany's investments require relatively few imports, as the country is a large producer of coal, steel and equipment. In addition, most of the industrially produced essentials on the German consumer's shopping list are being produced in Germany at competitive prices, thus excluding their importation. Only in the agricultural sector is there a considerable amount of tariff protection. Clearly, in its absence, and even more importantly in the absence of the German system that raises the price of imported agricultural products to the higher price level of domestically produced goods, German agricultural imports would be considerably larger. But price protection of agriculture is deeply ingrained in the German economy, and may be considered, as in other nations, a rather permanent feature. Germany's comparatively low propensity to import therefore appears to have rather basic structural causes.

Because of the varying degrees of convertibility of the world's currencies, Germany's balance of payments, like that of many other nations, is compartmentalized. The special conditions that have prevailed, and are likely to prevail in the foreseeable future, in Germany's international transactions with, respectively, the dollar area, the European Payments Union area (EPU area), and the group of countries with which trade is settled on a strictly bilateral basis (the so-called bilateral-clearing-agreement countries) therefore require separate consideration (Table III).

A. *Dollar Area*

In the late 'forties, the dollar area,[3] and especially the United States, was Germany's largest source of imports. With exports to the area at a

[1] German export prices in the second half of 1953 were 22 per cent above the 1950 level, compared, for example, with Belgium-Luxembourg (10 per cent) and the United Kingdom (19 per cent).

[2] For a discussion of this interesting phenomenon, see Dr. Otmar Emminger, *Deutschland's Stellung in der Weltwirtschaft,* Kieler Vorträge, Neue Folge 4 (Kiel, 1953), p. 15.

[3] In the German statistics, which are used in this paper, the dollar area includes (in addition to the United States and Canada) a number of countries in Central and South America,

very low ebb, Germany was running high dollar-area deficits on current account, which were financed by United States aid ("Government and Relief in Occupied Areas," and the European Recovery Program). Since then, however, Germany has made remarkable progress in closing

TABLE III.—GERMAN BALANCE OF PAYMENTS POSITION ON CURRENT ACCOUNT
(millions of dollars)

	Exports Goods and Services	Imports Goods and Services	Balance
All areas:			
1949	1,282.7	2,304.2	−1,021.5
1950	2,199.1	2,823.7	− 624.6
1951	3,896.0	3,752.0	+ 144.0
1952	4,814.0	4,253.0	+ 561.0
1953	5,316.9	4,379.8	+ 937.1
Dollar area:			
1949	152.6	1,078.3	− 925.7
1950	316.9	589.8	− 272.9
1951	475.6	864.9	− 389.3
1952	696.0	788.0	− 92.0
1953	920.8	673.3	+ 247.5
EPU area:			
1949	1,046.0	1,078.0	− 32.0
1950	1,617.6	2,022.6	− 405.0
1951	2,859.5	2,383.2	+ 476.3
1952	3,410.0	2,883.0	+ 527.0
1953	3,696.7	3,128.8	+ 567.9
Bilateral-clearing countries:			
1949	84.1	147.9	− 63.8
1950	264.6	211.3	+ 53.3
1951	560.9	503.9	+ 57.0
1952	708.0	582.0	+ 126.0
1953	699.4	577.7	+ 121.7

Source: Bank Deutscher Länder.

the dollar gap. The value of German exports of goods and services in 1953 was about six times as large as in 1949, while imports declined over the period by about 40 per cent. Over this period Germany was able to lower her deficit on trade account from $979 million in 1949 to $48 million in 1953. Even more strikingly, as a result especially of United States troop expenditures in Germany (which increased from $43 million in 1949 to $235 million in 1953), she achieved in the last

such as Cuba, Mexico, Panama, Peru, and Venezuela, as well as a number of miscellaneous countries in Eastern Europe, Africa, and Asia that do not clear through the EPU and with which no bilateral-clearing agreements have been concluded. This miscellaneous group includes such countries as China, Rumania, and the Soviet Union, but trade with them is extremely small.

year a total current-account surplus vis-à-vis the dollar area of $247.5 million. However, if it had not been for the troop expenditures and a small amount of foreign aid,[4] the country would have roughly achieved balance with the dollar area.

On the import side, the improvement in Germany's trade balance was brought about by increasing the production of such goods as coal and wheat, which had been imported from the dollar area on a large scale, and by meeting import requirements increasingly in other regions, especially the EPU area. Through her system of import licensing, Germany has been in a good position to direct her imports of goods and of services (such as shipping) to areas in which her current-account position is strong. She has, moreover, saved dollars by triangular transactions; dollar commodities have been procured increasingly by way of transit imports from other areas ($156 million in 1952 and $173 million in 1953), especially through EPU countries, with the effect that in 1953, 23 per cent of the imported dollar-area commodities were purchased in countries other than the dollar area.

On the other hand, with a view to promoting exports to the dollar area, Germany inaugurated in 1950 a dollar-retention scheme, which, in slightly different forms and with temporary interruptions, was continued through December 1953. In its latest form the scheme involved the issuance of so-called "dollar import rights" to German exporters to the dollar area for a proportion of their exports, which rights they were able to sell at a premium to potential importers from the area. The scheme, therefore involved a unilateral and partial devaluation of the D-mark vis-à-vis the dollar, the degree depending on the premium that the rights commanded in the market. In view of the fact that the scheme was criticized by the International Monetary Fund and that Germany's dollar position had greatly improved in the course of 1953 (thus no longer warranting special incentives for exports to the dollar area), the scheme was abandoned.

Encouraged by her improved dollar position, Germany as of February 17, 1954 freed from quantitative restrictions some 2,000 of the 6,000-odd items in her foreign trade statistics, representing, according to official German estimates, some 40 per cent of the value of goods imported in "private" (non state) trading from the dollar area in 1953, and some 30 per cent of the value of all goods imported from that area in that year.[5] The liberalization measure is expected by German authorities to increase direct dollar imports by an estimated amount of 50 to 70

[4] United States aid to Germany amounted to $923.3 million in 1949, and declined subsequently to $114.5 million in 1952 and $63 million in 1953.

[5] The main freed items were cotton, tobacco, and several important metals, as well as certain types of machinery, electrical goods, precision tools, and chemicals.

million dollars in 1954.[6] German spokesmen have indicated that, if all goes well, the liberalization list will gradually be broadened.

As regards the impact of more liberal dollar imports on nondollar countries, it should be recalled that some of the commodities included in the liberalization list, such as cotton, were already being imported to some extent, although at higher prices, for example from bilateral-clearing countries (*e.g.*, cotton from Brazil), or else by way of transit imports, chiefly through other EPU countries and paid for in their currencies. Moreover, by increasing her direct imports, say of cotton, from the dollar area at prices lower than those previously paid in soft-currency areas, Germany not only may improve her terms of trade but also may become more competitive in the world markets for her exports, say, of textiles. For all these reasons, the liberalization of imports from the dollar area, especially if the liberalization list should be broadened, may therefore tend to make Germany's creditor position vis-à-vis both the EPU and the bilateral-clearing countries somewhat more extreme, and may also tend to increase the inflow of EPU dollars into Germany.

Germany's over-all position vis-a-vis the dollar area in 1954 and thereafter will be influenced not only by her dollar-import liberalization move but also, and even to a larger extent, by the resumption of transfers on her large foreign debt under the London Debt Agreement, and of transfers in regard to blocked foreign assets.[7] Germany, on the other hand, hopes to further improve her position vis-à-vis the dollar area, for example by offshore defense orders for equipping the forces of the United States and other North Atlantic Treaty Organization countries (or possibly those of Germany herself if she should be allowed to rearm). To date, very few such contracts have been placed with German firms, and the German government reportedly has been pressing for larger orders. Moreover, the outlook for continued dollar receipts from United States troops stationed in Germany appears favorable; such receipts are likely to continue, whether the European Defense Community comes into being or not. Political conditions so far have favored Germany's progress toward the closing of her dollar gap, and regardless of the ultimate fate of the EDC, and barring a major recession in the United States, the prospects are that she will make still further progress in this direction.

[6] That the increase in dollar imports may be considerable is indicated by the fact that, in the first five months of the current year, permits for imports from the dollar area averaged $55 million per month, as compared with almost $40 million during the same period in 1953, the increase amounting to more than 37 per cent.

[7] For a discussion of Germany's newly assumed transfer obligations in the capital sector see Section III.

B. *European Payments Union Area*

Traditionally, the largest proportion of German exports has gone to markets in Western and Northern Europe, and it is therefore not surprising that in this area Germany has made her greatest strides since the war. The European Payments Union area[8] is at present Germany's largest trading area, accounting in 1953 for more than 70 per cent of both her merchandise exports and imports. The increase in her current account transactions with this area has been spectacular: Exports of goods and services to the EPU area in 1953 were 3.5 times as large as in 1949, and imports from that area almost 3 times as large. Simultaneously, as already indicated, there has occurred a remarkable shift in German imports from the dollar to the EPU area. While in 1949 each area provided about 47 per cent of Germany's imports of goods and services, the share of such imports from the dollar area declined to about 15 per cent in 1953, while that of the EPU area rose to about 70 per cent. Germany's dollar-import liberalization move may tend to lower that ratio in favor of the dollar area.

It will be recalled that in the early stages of the European Payments Union (which was established July 1, 1950), Germany ran large deficits with the Union (Table IV). In the period from July 1950 through February 1951 she incurred a cumulative deficit of $457 million, which cost her a large amount of dollars ($174 million), made her the EPU's largest debtor ($283 million), and threatened the very existence of that organization. The deficit was caused chiefly by the swift action of German importers in piling up raw materials before prices rose to the post-Korea peak, and possibly by the belief held at that time in certain quarters that sterling might be appreciated. However, stringent measures on the part of Germany's central bank in stopping the issue of licenses for imports from EPU countries, combined with a raising of the discount rate and of reserve requirements and a subsequent drastic reduction in bank credits, quickly redressed the situation. Since March 1951 the monthly EPU accountings have shown German surpluses almost continuously, and at the end of April 1953, with a credit balance of $292 million, Germany was for the first time the largest creditor of the EPU—a position she has held to date. The magnitude of the upswing is indicated by the fact that, in the period from March 1951 through June 1954, Germany improved her EPU position by $1,565 million: she recovered $174 million that she had paid to the EPU during

[8] The EPU area includes the member countries of the Organization for European Economic Cooperation (OEEC) and the dependent territories of Belgium, France, the Netherlands, and Portugal. In addition, it includes the dependent territories of the United Kingdom, as well as the other sterling area countries, such as Australia, Burma, Ceylon, India, New Zealand, Pakistan, Iraq, Southern Rhodesia, and the Union of South Africa.

TABLE IV.—GERMAN CUMULATIVE POSITION WITH THE EUROPEAN PAYMENTS UNION

(millions of dollars[a])

As of End of	Cumulative Accounting Surplus (+) or Deficit (−)	Credit Extended to (+) or by (−) EPU	Gold and Dollars Received from (+) or Paid to (−) EPU
1950—September	−173.4	−142.4	− 31.0
December	−356.7	−216.5	−140.2
1951—March	−445.8	−272.1	−173.7
June	−272.8	−182.6	− 90.2
September	−106.0	−104.8	− 1.2
December	+ 43.3	+ 43.3	—
1952—March	+135.1	+117.5	+ 17.6
June	+311.1	+205.6	+105.5
September	+443.2	+271.6	+171.6
December	+377.9	+239.0	+138.9
1953—March	+441.2	+270.6	+170.6
June	+577.3	+338.6	+238.7
September	+660.7	+380.3	+280.3
December	+821.2	+460.6	+360.6
1954—March	+990.2	+545.1	+445.1
June	+1,107.5	+603.7[b]	+503.8

[a] Claims of European Payments Union countries against each other are expressed in "accounting units" which are equivalent to United States dollars.
[b] As regards repayments on the credits, see text.
Source: OEEC press releases.

the deficit period; acquired additional dollars to the amount of $504 million; paid off EPU credits of $283 million; and became a net creditor of the EPU to the amount of $604 million.

The pattern of Germany's payments in the EPU area can be briefly stated. If we disregard the period from July 1950 through March 1951, Germany has been running persistent surpluses with all member countries except the United Kingdom and the Netherlands. With the latter countries she has been running deficits, those with the United Kingdom looming particularly large; they are due chiefly to imports of raw materials from overseas (including transit imports), for which payment is being made in sterling and Dutch guilders respectively. However, Germany's surpluses with the other countries have considerably exceeded her deficits with the United Kingdom and the Netherlands, with the result that Germany has built up large credit balances with the EPU and the latter has become a large source of dollar earnings. Therefore, the greatest benefits derived from the EPU have been the importation especially of sterling area commodities paid for with surpluses vis-à-vis other EPU countries, and the accumulation of dollars as a result of Germany's over-all surplus with the EPU.

Germany's EPU quota, originally established at $320 million, was increased as of July 1, 1951 to $500 million. However, since June 1953, when Germany's cumulative accounting surplus with the EPU first exceeded the $500 million mark, successive so-called *rallonges,* aggregating $300 million, have been added to the quota. Under these *rallonges,* which are in effect quota extensions, surpluses have been settled half by the granting of credit by Germany and half in dollar payments by the EPU to Germany. However, Germany's cumulative accounting surplus by the end of 1953 already exceeded the total of $800 million (quota plus *rallonges*), and monthly EPU surpluses of Germany have since been settled in the same way on a 50/50 basis.

With additional credits extended to EPU nations every month—they aggregated the equivalent of more than $460 million by the end of 1953—there was mounting opposition in Germany last year toward extending, by way of the EPU, automatic and "anonymous" credits to such nations as France and the United Kingdom; it was regarded as more in the German interest to export long-term capital to underdeveloped nations, say in Latin America, especially in the form of direct investment. Such capital exports, unlike the "anonymous" credits, would give Germany a measure of control, it has been asserted, and would lead indirectly to a broadening of the markets for her exports in these areas. Moreover, it has been argued by German spokesmen that the automatic credit extensions that the EPU mechanism involves have relieved some debtor nations of pressure to pursue anti-inflationary policies, and have allowed them to maintain overvalued exchange rates favoring imports and discouraging exports. Moreover, there is concern in Germany lest the credit extensions, which are financed directly by her central bank, engender inflationary pressures within Germany.

Notwithstanding these reservations, the benefits derived from the EPU in the form of dollar receipts, imports of overseas commodities, and absence of discrimination against German exports to the extent that other EPU nations have liberalized their imports, have been clearly recognized by Germany, especially by her central bank. Therefore, in the discussions preceding the extension of the EPU for one year from July 1, 1954, Germany favored the proposal. However, supported by Belgium, the Netherlands, and Switzerland, she has been pressing for a higher proportion of gold and dollars in the monthly EPU settlements of extraquota surpluses, say, at the ratio of 65 to 35, and for a plan under which claims that are eighteen months old or more would have to be repaid within, perhaps, a period of three years. However, the EPU was eventually renewed, with the basic proviso that all current monthly surpluses and deficits, respectively, of all the EPU nations will henceforth be settled one-half in dollars and one-half in credits. Nevertheless, as regards credits granted to the EPU, the OEEC decision extending the organization through June 1955 provided for immediate dollar payments by the major debtors of part of their debts; the consolidation through bilateral arrangements of parts of the remaining debts; and the reimbursement from EPU dollar funds, originally contributed by the United States, of part of the credits extended by the surplus countries.[9]

There still remains the basic problem of Germany's persistent monthly EPU surpluses, which in 1953 ran at the monthly rate of some $40 million. Further action on the part of Germany to lower her EPU surpluses is limited by the fact that, as already stated, she has resumed service on her foreign debt and in addition has assumed considerable transfer commitments in regard to blocked assets; all these transfers obligations will benefit EPU countries even more than dollar countries (see Section III). Most important, she has liberalized imports from EPU countries to a very high degree.

Germany, which at the time of her balance-of-payments crisis at the end of February 1951, had suspended all previous liberalization measures vis-à-vis EPU nations, resumed liberalization after December 1951. Since then she has gradually freed from quota restrictions her trade with EPU countries with the result that since April 1953 about

[9] As a result of subsequent arrangements, Germany, at the time of the June settlement, received—in addition to the dollar receipts which the monthly settlement involved—from individual debtors of the EPU an amount of some $70 million (including $35 million from the United Kingdom), and an additional $70 million out of EPU resources. Her credits extended to the EPU, amounting to the equivalent of some $600 million by the end of June, were thus reduced to around $460 million. In addition, also as a result of bilateral arrangements with individual EPU debtor nations, Germany will receive from such nations an amount of about $200 million (including $105 million from the United Kingdom) in monthly installments, generally over a period of seven years; but these amounts remain part of Germany's claims against the EPU to the extent that they have not been paid.

In addition to the (adjusted) credits extended to the EPU of the equivalent of some $460 million, Germany undertook to extend further credits to the EPU to the amount of $300 million. Since all further German EPU surpluses will be henceforth settled half in dollars and half in credits to the EPU, no new arrangements would have to be made until Germany, if she were to run further surpluses, has received additional payments from the EPU to the amount of $300 million and has extended credits to the EPU totalling some $760 million. While quotas and rallonges have been adjusted and formally retained under the new EPU provisions, they no longer have their earlier significance in view of the already mentioned provision that all current monthly surpluses and deficits, respectively, will be settled on a 50/50 basis.

90 per cent of this trade has been free from such restrictions.[10] A considerable margin for further liberalization in the trade sector appears to exist only as regards imports of food and feeds, but resistance on the part of German agriculture, which has the support of the German government, makes substantial further liberalization in this sector (as well as the lowering of agricultural tariffs) unlikely.

With her comparatively high liberalization ratio, Germany belongs now to the group of countries—Belgium-Luxembourg, the Netherlands, Italy, Portugal, Sweden, and Switzerland—that have liberalized their European trade by some 90 per cent or more. She compares favorably, moreover, with the United Kingdom which has liberalized to date to the extent of 79 per cent, and with France whose present liberalization ratio is 53 per cent.[11] In view of Germany's comparatively high liberalization ratio, the Economic Committee of the OEEC, in investigating the causes that have led to Germany's extreme creditor position in EPU and in making recommendations on how this situation might be remedied,[12] could scarcely recommend further liberalization measures with a view to increasing German imports. The committee proposed essentially the adoption by Germany of *internal* measures directed toward expanding both consumption and investment and thereby increasing the German demand for imports.[13]

C. *Bilateral-Clearing Countries*

In the prewar period Germany made great efforts to promote trade with the less developed countries of the world, whose economies are

[10] The ratio for food and feeds was 79.4, for industrial raw materials 97.8, and for industrial finished products 93.8. Doubt has been expressed as to whether these ratios are realistic because they are based on German imports in 1949 when the composition of imports from EPU countries was different. A recomputation of the liberalization ratios in terms of German imports in 1952, however, has given rather similar results. The over-all figure for liberalized imports, on the recomputed basis, was 89.3 per cent, compared with 90.1; and the percentages for the three major commodity categories were respectively 82.4, 94.5, and 87.4. As in other countries, the liberalization figures of course refer only to so-called private imports, thus excluding imports by state organizations, which in the German case are important in the agricultural sector. If state trade were included in the base, the liberalization ratio for food and feeds in 1952 would have been only about 60 per cent. On these data, see the article, "Die missverstandene Liberalisierungsquote," *Deutsche Zeitung,* August 8, 1953.

Effective February 1, 1954, Germany has freed from quota restrictions a number of imported items that had not been imported in 1949. This liberalization move therefore did not change the over-all liberalization ratio of 90.1 per cent (on a 1949 base), but, using a 1952 base, the over-all ratio would be 91.4 per cent.

[11] However, all these comparisons, which are of July 1954, should be taken with a grain of salt not only because the liberalization ratios refer exclusively to private trading, thus excluding state trading, which varies in importance from country to country, but also because the different countries maintain varying degrees of tariff protection, which is of course as much of a trade barrier as import quotas.

[12] See, *Report* by the Economic Committee of the OEEC on the Causes of Disequilibrium in the EPU which have led to Germany's Extreme Creditor Position, Paris, April 13, 1954.

[13] For a more detailed discussion of these proposals see below, Section IV.

complementary to her own and which supply both a market for her industrial products and a valuable supplementary source for her requirements of raw materials and foodstuffs. Germany has resumed, if on a modest scale, trade with such countries in Eastern Europe and has pushed trade with Latin American countries as well as with other countries that belong to neither the dollar area nor the EPU area. With the seventeen members of this rather heterogeneous group Germany has concluded bilateral-clearing agreements, with credits by either side extended to the same amount—the so-called swing limit—and with the characteristic provisions that debit balances exceeding the swing limit be settled in dollars.

In 1953, Germany's exports of goods and services to this group were 8.3 times as large as in 1949, but imports from this group were only about 4 times as large. This disparity in expansion reflects in particular the strong demand for German capital goods from countries in the process of industrialization, as well as their inability, concomitantly with their industrialization efforts, to provide raw materials and foodstuffs for export at competitive prices. "Over-importing" by certain members of this group was of course facilitated by the strong desire on the part of German industry to recoup export markets, especially in Latin America.

With imports lagging behind, the upsurge of German exports to these countries, especially in Latin America, led in 1952 to an increase in German net clearing balances with the group of the equivalent of more than $200 million (Table V). Last year, however, the foreign exchange authorities of the importing nations exercised more restraint in issuing licenses for imports from Germany, and in addition, German exporters, who found it increasingly difficult to cover their exports by credit insurance, showed more caution. Since September 1953, when balances reached a peak of $226 million, they have shown a declining trend.

A special case is that of Brazil, which in 1952 built up a clearing debt against Germany of the equivalent of more than $90 million, thus exceeding the swing limit of $13.5 million by some $78 million, without however settling the difference by dollar payments. With a view to discouraging imports from Brazil and encouraging exports to that country, Germany in early September 1952 inaugurated a scheme authorizing a free market in Germany for clearing claims against Brazil, and allowing German importers from Brazil to pay 80 per cent of the invoice value with clearing claims bought from exporters in the market, while the remainder is to be paid with clearing claims acquired at the official clearing rate. Since Brazilian clearing claims are traded at a discount (about 8 per cent in June 1954), the scheme

TABLE V.—GERMAN BALANCES WITH BILATERAL-CLEARING COUNTRIES
(millions of dollars;[a] minus sign indicates German debit balances)

	Swing Limits as of June 30, 1954	December 1951	December 1952	December 1953	March 1954	June 1954
All countries	195.1	−20.1	185.2	212.6	191.0	173.3
Latin America[b]	86.5	−35.5	84.5	120.0	107.3	97.0
of which:						
Argentina	50.0	−33.3	−7.4	33.1	38.0	33.2
Brazil	13.5	− 4.2	91.9	78.6	63.0	59.1
Eastern Europe[c]	57.3	28.3	65.3	37.4	46.0	36.8
of which:						
Finland	20.0	− 2.4	27.9	11.7	10.6	8.3
Yugoslavia	17.0	10.0	17.4	11.5	16.9	10.5
Other countries	51.3	−12.9	35.4	56.2	37.7	39.5
comprising:						
Egypt	15.0	− 0.5	9.9	18.2	7.0	9.3
Iran	8.0	− 0.1	8.2	4.5	4.5	7.2
Japan	12.0	−10.5	−0.1	14.6	13.5	12.8
Spain	16.3	− 1.8	17.4	18.9	12.7	10.2

[a] The United States dollar is the accounting unit in which the claims against each other of the countries engaged in the bilateral clearings are expressed.
[b] Seven countries: Argentina, Brazil, Chile, Colombia, Ecuador, Paraguay, and Uruguay.
[c] Six countries: Bulgaria, Czechoslovakia, Finland, Hungary, Poland, and Yugoslavia.
Note: Figures are rounded and do not necessarily add up to the totals.
Source: Bank Deutscher Länder.

involves in effect a unilateral depreciation of the Brazilian cruzeiro by Germany; this is indeed a strange reversal of Germany's position as compared with that in the early 'thirties when she was "over-importing" from such countries as Brazil and the so-called Askimarks were at considerable discounts. Brazil, moreover, committed herself to issuing export licenses at a higher rate than import licenses. Finally, the rise in the price of coffee contributed further to remedying the situation, with the result that, beginning in 1953, German clearing claims against Brazil have shown a declining trend.

Generally speaking, greater balance in Germany's trade with the clearing-agreement countries has been sought either by renegotiation, as in the cases of Brazil and Yugoslavia, or by action on the part of Germany's foreign trade partners such as Chile, which stopped the issuing of import licenses when the swing limit had been exceeded. Moreover, when a contracting country had exhausted its swing limit, Germany has instituted "waiting lists" for the out-payments of D-marks to exporters.

German spokesmen have expressed dissatisfaction with the development of the clearing arrangements. The clearings were instituted, it has been claimed, rather as transitory expedients for meeting payment difficulties resulting from exchange shortages on the part of Germany and of the partner countries, but have deteriorated into a system under which foreign countries are in effect receiving long-term credits. There has therefore been a noticeable tendency on the part of Germany to reduce swing limits, and she is considering wider use of a plan under which, as in her latest agreement with Spain, the swing limits would be adjusted periodically so as to be more in conformity with the lower side of the commodity exchange, which in most cases represents German imports. Germany is reportedly aiming at the ultimate replacement of bilateral trading by trade on a dollar basis, but she is also aware of the fact that quite a few countries may not be able to afford dollar payments in the foreseeable future.

Prior to the war, especially before the advent of the Hitler regime, Germany traded on a major scale with the Soviet Union, which reportedly was most punctilious in meeting its financial obligations. Moreover, Germany before the war cultivated trade with other nations in Eastern and Southeastern Europe—a trade that was even more important during the war, when invasion or political penetration gave her a dominating position in the trade of these countries. Trade with these nations is of course running at present at a very low level; and the little trade that persists takes place in the form of transit trade through third countries, or is being settled on a bilateral-clearing basis or in dollars—the Soviet Union and China, for example, being classified as "dollar countries." Consequently, German industrialists, remembering their former profitable experiences, have been pressing for some time for an expansion of trade with the Soviet bloc countries. To date, however, little has been achieved in increasing trade with these countries, with China, beginning in 1953, representing a notable exception.[14]

D. *Transferable-Account Area for the D-Mark*

Germany as of April 1, 1954 established a link between the EPU area and the bilateral-clearing countries by authorizing the institution of "limited convertible D-mark accounts" which are devised for transactions with countries of the combined EPU and clearing-agreement group. Generally speaking, these accounts may be credited with the

[14] Exports to China increased from the equivalent of $2.8 million in 1952 to $25 million in 1953, while imports increased over this period from $17.6 million to $33.3 million, a large proportion of the imports in 1953 having been imported in transit by way of Hong Kong and having been paid for in sterling through EPU.

proceeds of exports of goods and services to Germany for which payment, either via the existing (bilateral or multilateral) clearing arrangements or in freely convertible currency, has been authorized by Germany.[15] Balances on these accounts can be used for paying for imports of goods and services from Germany, and in addition can be used for making payments, via the existing bilateral or multilateral clearings, to any EPU or bilateral-clearing country. In this way, Germany created what may be called a "transferable account area for the D-mark." For example, an exporter in a bilateral-clearing country —say, Argentina—may (the Argentine exchange authorities permitting) open a limited convertible D-mark account, may have the mark proceeds of his exports to Germany credited to such an account, and may remit them, via the EPU, to a Belgian exporter to Argentina (assuming that the Belgian foreign exchange authorities permit acceptance of such payment). Transferability is also assured by the provision that balances may be freely transferred from any limited convertible D-mark account to any other.

However, while D-mark claims are transferable as among the countries of the combined EPU and clearing-agreement group, conversion of such funds into dollars has been excluded: simultaneously with authorizing limited convertible D-mark accounts, Germany also authorized institution of "freely convertible D-mark accounts," which may be credited with the proceeds of exports of goods and services to Germany for which payment in freely convertible currency has been authorized by Germany. Balances on these accounts are to be convertible into dollars, as well as into any of the currencies of the EPU and clearing-agreement countries.[16] However, while balances may be transferred from a free D-mark account to a limited D-mark account, transfers from a limited account *to* a free account have not been authorized, in order to keep EPU and bilateral-clearing countries from converting their mark balances into dollars.

[15] The proceeds of exports of goods and services to Germany from Brazil, Turkey, and Yugoslavia cannot be credited to such accounts.

[16] Prior to authorization of these accounts, German trade with the dollar area had been settled exclusively in dollars through dollar accounts, the claims arising from German exports having been credited, and the liabilities arising from German imports having been debited, to such accounts. The institution of free D-mark accounts makes it possible also to transact German trade with the dollar area, through the latter accounts, in terms of marks. Since mark balances on these accounts are to be convertible into dollars at the official D-mark rate, it will be a matter of indifference on purely economic grounds to exporters from the dollar area whether they receive payment in dollars or in convertible D-marks—unless they anticipate depreciation of the mark, which does not seem at present to be in prospect. The fact that the mark balances can be converted into any nondollar currency does not, of course, give foreign exporters to Germany any advantage, since they have always been able to convert their dollar receipts into any nondollar currency.

Reports that the establishment by Germany of a transferable D-mark account area was prompted by Britain's change in its exchange regulations, effective March 22, 1954, which merged the bilateral-sterling account area into the transferable-sterling account area, appear to be inaccurate in view of the facts that the forthcoming German move had been openly discussed for some time in the German press, and that the announcement was delayed because certain technical arrangements had first to be completed. It is also inaccurate to say that the German authorization of free and limited D-mark accounts is more far-reaching than what Britain, over a period of years, has done; free D-marks correspond to American-account sterling, and limited D-marks correspond to the now broadened transferable-account sterling.

As regards possible shifts in payments and trade patterns that the initiation of limited convertible accounts may bring about as between the EPU area and the bilateral-clearing area, the chances are that funds will tend to flow from the countries with softer currencies to those with harder ones; one may therefore anticipate an outflow, even if moderate, of funds from certain clearing-agreement countries to certain EPU countries. If this should occur, Germany's claims against bilateral-clearing countries would tend to rise, while her claims against EPU countries would tend to decline, or to rise at a slower rate. However, an outflow of funds from the bilateral-clearing countries would require permission from their foreign exchange authorities, and would be limited by the fact that most of these countries have already reached, or are close to, their swing limits; when their debit balances with Germany exceed these limits, they will have to settle the excess in dollars. Their exchange authorities would therefore tend to discourage a further outflow of funds if it seemed likely to lead to a situation where the swing limit would be exceeded.

II. *The Rise in Gold and Foreign Exchange Reserves*

Liberal United States aid and, since 1951, Germany's increasingly favorable balance of payments have been reflected in large increases in her gold and foreign exchange reserves (see Table VI). Accruals to her gold and dollar reserves in 1950—there were small dollar losses in 1949—were a by-product of United States aid, which exceeded Germany's current-account deficit with the dollar area by a substantial amount; this situation continued in 1951 and 1952, although at a progressively declining rate. However, since 1952 surpluses with the EPU have become, as previously stated, an important source of dollars. In 1952 about one-half of the increase in gold and dollar reserves was earned from the dollar area, and one-half from the EPU area;

in 1953, when Germany's surplus with the dollar area greatly increased, about 60 per cent of the improvement resulted from transactions with the dollar area and about 40 per cent from transactions with the EPU area.

By the end of 1953, Germany, which started virtually from scratch at the time of the currency reform, had built up gold and dollar reserves equivalent to more than 3½ months of imports from all areas. On this basis, they were comparable, as already stated, with those of, for example, the sterling area. It should be noted that of Germany's

TABLE VI.—GERMAN GOLD AND FOREIGN EXCHANGE HOLDINGS

(millions of dollars, or dollar equivalent; minus sign indicates net liabilities)

	December 1950	December 1951	December 1952	December 1953	March 1954	June 1954
Gold	—	28	140	325	387	408
Dollars	148	338	497	844	953	1,041
Gold and Dollars	148	366	637	1,169	1,340	1,449
EPU account	−192	—	253	424	509	567
Other claims against EPU Countries	−116	23	28	140	133	118
Bilateral Accounts	24	−26	187	213	191	173
All Reserves	−136	363	1,105	1,946	2,173	2,307

Source: Bank Deutscher Länder.

total gold and foreign exchange reserve at the end of 1953 only the gold and dollar portion, or about 60 per cent, was fully convertible, while the remainder had only limited area convertibility or was wholly inconvertible.

Finally, Germany's foreign exchange position has been potentially strengthened by her joining in August 1952 the International Monetary Fund, from which she may purchase dollars and other foreign currencies. Germany's Fund quota is $330 million: under the statutory provisions of the Fund Agreement she may buy foreign currencies within any 12-month period to the amount of $82.5 million, while the cumulative amount of purchases is not at any time to exceed $408 million (quota plus gold contribution). These "drawing rights," like those of other Fund members, are practically automatic only to the amount of Germany's gold contribution (at present $78 million), and every further purchase has to be negotiated with the Fund.

III. *The Resumption of Transfers in the Capital Sector*

Germany's balance-of-payments position, vis-à-vis both the dollar area and the EPU area, will be increasingly affected by the resumption of transfers in connection with her large foreign obligations, which amounted by the end of 1953 to the equivalent of $7.4 billion (see Table VII). A large proportion of these obligations consists of private and public debts incurred in the 1920's, and of foreign investments, such as direct investments, real estate holdings, and portfolio investments, most of which had been made during the same period. In the early postwar years, foreign aid, especially that of the United States, added substantially to these amounts. Later, Germany recognized further obligations both toward Israel and toward refugees from the Hitler regime.

TABLE VII.—GERMAN FOREIGN DEBTS AND FOREIGN INVESTMENTS IN GERMANY AT THE END OF 1953

(millions of D-marks or D-mark equivalent)[a]

	Total	Dollar Area	EPU Area
Settled by London Agreement:			
Prewar debts	7,230	2,225	4,625
Postwar debts	6,770	4,955	1,815
Total	14,000	7,180	6,440
Foreign investment in Germany, not covered by London Agreement	9,720	2,925	6,730
(Of which: investments out of blocked marks)	(1,490)	(525)	(930)
Blocked mark balances with German banks	790	260	480
Restitution obligations:			
Agreement with Israel[b]	3,210	2,910	300
Claims of foreign individuals	3,400	2,370	1,020
Total	6,610	5,280	1,320
Grand Total	31,120	15,645	14,970

[a] The official rate to the dollar is 1 D-mark=0.2384 dollars.
[b] Amount outstanding as of the end of 1953.
Source: Bank Deutscher Länder.

In the early 1930's, it will be remembered, Germany stopped the transfer of interest and amortization on all foreign debts previously incurred and of earnings on all foreign investments previously made in Germany; since that time all such investments and the earnings thereon have been blocked. Since March 1951 owners of blocked investments have been able to liquidate them within Germany and, after the proceeds had been credited to a blocked mark account, to sell such proceeds to other residents abroad by way of the blocked mark trade in such financial centers as London, New York, and Zurich. In this way, the owners were able to achieve a "transfer" of their funds, although at a loss since blocked marks have been traded at a discount. Residents abroad acquiring the blocked mark balances could use them chiefly for making investments in Germany, which in turn were blocked. Any earnings on foreign investments either were reinvested or accrued to the blocked mark balances, and could be "transferred" in the same way at a discount by way of the blocked mark trade.

The decisive step in resuming transfer, at the official rate, of interest and amortization charges on Germany's large foreign obligations was the conclusion of an international agreement signed in London on February 27, 1953 and made effective on September 16, 1953 which provided for the resumption of interest and amortization payments on Germany's contractual prewar debt—most of which had been incurred in foreign currencies—as well as on all of her public postwar debts. The initiative for this settlement was taken largely by the creditor nations, but met with Germany's cooperation, since she wished to restore her international standing. Under the London Agreement interest payments were to be resumed in 1953, while amortization has been postponed until 1958, with the last interest and amortization payments to take place as late as 1994.[17]

Moreover, by a special agreement with Switzerland of August 26, 1952 and a subsequent arrangement, Germany settled the wartime clearing debt to that country. Part of the Swiss claims was funded into two 20-year loans, while the remainder is to be amortized over some 30 years. Of a still different nature is the reparations agreement of September 19, 1952 concluded with Israel, under which Germany has committed herself to deliver goods to Israel over a period of 12 to 14 years up to the equivalent of $821 million. Part of the deliveries are being procured in Germany and part, chiefly petroleum, in the sterling area. In addition, Germany has passed legislation providing for compensation for refugees from the Nazi regime, and has made arrangements for the transfer of their compensation claims.

After the London Agreement came into effect, Germany moreover authorized, by a number of successive steps, the transfer at the official rate of virtually all earnings on foreign assets blocked in Germany, irrespective of the area in which their recipients reside, thus taking a decisive step towards keeping blocked mark balances from increasing further. In addition, Germany has made possible the *direct* conversion at the official rate, into the currencies of their owners, of all blocked mark balances on deposit with West German banks on

[17] On the London Agreement, see my article, "Some Basic Aspects of the German Debt Settlement," *Jour. Finance*, Sept. 1953, VIII, 298.

March 31, 1954 that are owned by residents of the EPU area or of the bilateral-clearing countries. Finally, blocked balances held by the original owner and not exceeding 10,000 D-marks on December 31, 1953 may be transferred in full at the official rate, without distinction, to all areas, including the dollar area.[18]

The transfer obligations assumed under the London Agreement and under the agreements concluded, respectively, with Switzerland and Israel, as well as the obligations assumed in regard to foreign assets blocked in Germany, will of course tend to decrease Germany's surplus both with the dollar area and the EPU area. As a result of delays in the completion of certain technical arrangements, exchange outlays in 1953 resulting from obligations assumed under the London Agreement were comparatively minor. However, the agreement and all the mentioned commitments may involve a transfer burden in the current year the equivalent of roughly \$640 million; this figure includes a considerable backlog for payments of interest and earnings that were due but could not be made in 1953, as well as very rough estimates for capital transfers as a result of the unfreezing of blocked mark balances. Of the \$640 million, \$180 million, or less than 30 per cent, may have to be transferred to the dollar area, and \$460 million, or more than 70 per cent, to the EPU area. However, these estimates, especially as regards transfers to the EPU area, may prove to be on the high side; experience has shown that, generally speaking, residents of the EPU area are less eager to withdraw balances or transfer earnings than are residents of the dollar area. Of special significance is the fact that Switzerland, in order not to increase further her already extreme creditor position vis-à-vis the EPU, authorizes capital transfers from Germany only in exceptionally urgent cases; a large proportion of the blocked mark balances owned by residents of EPU countries are owned by residents of Switzerland or are registered in Swiss names.

While the regulations issued to date must be considered as first important steps in unfreezing blocked assets and in keeping them from increasing further, it should be kept in mind that they relate exclusively to the transfer of earnings on blocked assets and the transfer of

[18] Blocked mark balances existing on March 31, to the extent that they were owned by residents of the *dollar* area, cannot be converted directly into dollars at the official rate. In order to be converted into dollars such balances may be sold, as usual, by way of the blocked mark trade directly for dollars, or they may be sold, say, for sterling to residents of the transferable D-mark account area, in which case they can be transferred to a limited D-mark account of the new owner. In the latter case, conversion into dollars requires a second step, namely the sale for dollars of the currency received—for example, transferable sterling.

blocked bank balances, while the greater part of the blocked assets—consisting of direct foreign investments, real estate holdings, and other investments of a more or less long-term character—have remained blocked.

The outlook for unfreezing, step by step, all blocked assets appears to have greatly improved. A few years ago the threat of wholesale capital repatriation and capital flight was believed to be very real. However, German authorities appear at present to show less concern. The country does not seem any longer to be a "capital flight country," her surpluses being regarded, at least in some quarters, as due in part to an inflow of funds (some repatriation of capital, increased commercial credits, etc.). Of substantial weight is the consideration that a large proportion of the assets blocked in Germany consists of direct and other long-term investments, which their owners, in view of the stability of Germany's government, the prosperity of her economy, and her improved balance-of-payments position, may not wish to repatriate, especially since earnings are high and have now become transferable. Their owners might find it difficult to liquidate these assets (*i.e.,* turn them over at favorable prices into German hands); they also may well be deterred from doing so because they have long since written them off, and if they were to liquidate them and transfer the proceeds, high taxes on the resulting book profits would have to be paid. The psychological factor should also not be underestimated: the desire to repatriate assets is strong as long as repatriation is impossible, but weakens if repatriation is authorized.

There is also, of course, a considerable proportion of volatile assets. Germany's liberalization policy, as already stated, has focused to date on removing short-term claims, such as bank balances, and/or keeping new ones from arising; with the short-term claims out of the way, the blocked-asset problem may take care of itself. It is therefore quite possible that Germany, step by step, may unfreeze all blocked assets. This would do away with the blocked mark trade, and since the discount on blocked marks has been an obstacle to a net inflow of new foreign investments, a basic barrier to an influx of new capital would be removed. One may argue that, in spite of the comeback of the German economy and the improvement in Germany's balance-of-payments position, the foreign investment risk remains high as long as the East-West conflict remains unresolved. But investors, at least in Europe, appear to have learned to live under cold-war conditions. German experts may reason that, if a crisis were to develop and large-scale withdrawals were to threaten, Germany, which has developed considerable skill in the use of controls, could of course restore them in case they had been lifted.

IV. *D-Mark Convertibility Problems*

Germany, which since the days of the great depression had been faced with large balance-of-payments deficits, dwindling foreign-exchange reserves, and heavy discounts on the rates for her multitudinous categories of reichmark balances, finds herself at present in a rather strong position. Since she is running current-account surpluses with all areas, including the dollar area, and has extended large credits to both the EPU area and the area of the bilateral-clearing countries (aggregating the equivalent of $777 million by the end of June, 1954), foreign nations are now having to cope with what has been called a "D-mark shortage" or a "D-mark gap." Looking at it from Germany's side, her exchange problems are at present characteristically those of a surplus country: her problem is not so much to achieve D-mark convertibility, *i.e.,* to make foreign balances held with her convertible into dollars or other foreign currencies, but to make her own balances with foreign nations convertible into dollars or into D-marks. In short, Germany now faces a transfer problem in reverse.

The latter is indeed a serious problem. If D-mark shortages should persist, Germany may have to share the fate of other hard-currency areas or countries, in that she may be discriminated against by her foreign trade partners. They may—as they have already to some extent—restrict imports from Germany through trade deliberalization, the halting of imports and other measures. This would have serious effects on Germany's export industries, and accordingly on the further prosperous development of her economy as a whole. She is therefore anxious to maintain a high level of exports and avoid a situation where her trading partners might reduce their imports from her to the level of their exports to her.

It would accordingly benefit Germany indirectly if foreign countries, by following sound monetary and fiscal policies, and possibly by adjusting overvalued exchange rates, were to make their products more competitive in the German market, since German imports from them would then tend to rise. However, there is not much that Germany can do about this. In practice, she would have to rely primarily on her own policies to relieve D-mark shortages with a view to maintaining a high level of exports.

In this connection, Germany, it will be recalled, has followed a vigorous policy of trade liberalization; imports from the EPU area have been liberalized to the extent of 90 per cent, those from the bilateral-clearing countries to the extent of 80 per cent, and those from the dollar area to the extent of 30 to 40 per cent, with the over-all liberalization ratio for *all* areas amounting at present, according to official German estimates, to 80 per cent. Similarly, Germany has liberalized imports of invisibles to a high degree. The margin for further liberalization measures vis-à-vis the EPU area and the bilateral-clearing area is therefore relatively small, and German spokesmen hold that, for reasons of protection, the nonliberalized trade items may have to remain, for the time being, subject to quota restrictions. A considerable margin for further liberalization obviously still exists for imports from the dollar area, and Germany apparently wishes to permit further increases in imports from that area. It has been noted earlier, however, that the shifts in trade that such measures may bring about would tend to aggravate D-mark shortages of the EPU and clearing-agreement nations rather than relieve them.

Moreover, with a view to restoring her international credit and also to increasing her trading partners' capabilities to import from her, Germany, as stated earlier, has progressively removed restrictions on the transfer of earnings as well as of capital in regard to her large foreign obligations, and has in that way assumed large transfer obligations vis-à-vis both the EPU area and the dollar area. She may eventually be able to remove all restrictions on blocked assets, but the probable effect of all these measures in reducing D-mark shortages remains doubtful, since for a number of reasons foreign investors in Germany may decide to reinvest their earnings and not repatriate their capital.

In view of the fact that Germany made considerable progress in removing restrictions both in the trade sector and in the capital sector, the margin for further relaxations has become increasingly narrow. Moreover, the effectiveness of German measures of relaxation to date in closing the D-mark gap remains doubtful: although the measures of relaxation that have been taken, notably in the capital sector, are likely to decrease Germany's surpluses in the current year, especially vis-à-vis the EPU, current-account surpluses with that area are likely to persist, particularly after certain transfer backlogs in the capital sector have been taken care of during the present year.

With this situation in mind, attention has focused increasingly since last year on *internal* measures that Germany may take to increase her demand for imports both for consumption and for investment. The Academic Advisory Council to the Federal Ministry of Economics, in statements released on July 8, 1953 and January 16, 1954,[19] recommended that Germany, in order to maintain the current rate of economic growth (gross national product rose in 1953 by 6.8 per cent, as compared with 10.9 per cent in the preceding year) and to reduce balance-of-payments surpluses, with their concomitant automatic credit

[19] See, Bank Deutscher Länder, *Auszüge aus Presseartikeln,* July 10, 1953, No. 77, p. 2; and January 20, 1954, No. 8, p. 9.

extensions, pursue an economic policy of expansion directed toward increasing imports more rapidly than exports. To this effect, German economic policy should encourage, by way of credit expansion, an increase in domestic demand for foreign imports, especially of consumption goods. Also, with a view to increasing consumption, the council recommended a lowering of income tax rates, possibly combined with a raising of exemptions. The expansionist credit policy, finally, would contribute to a lowering of Germany's high level of interest rates and in that way contribute to the growth of investment. These recommendations have gained significance by the fact that the already-mentioned report of the Economic Committee of the OEEC has subscribed to their basic features. While not openly advising credit expansion, the OEEC report recommended "a policy for maintaining investment and intensifying the expansion of the economy by reduced taxation, which is already initiated, by lower interest rates and other appropriate means. This would have various advantages by reason of its effect on capital movements, investment, costs and, indirectly on consumption. . . . . Moreover, since the fraction of the national product devoted to consumption is relatively low, it would be reasonable to make use of the possibilities offered for raising consumption. . . ."[20] In this connection the Economic Committee approved of the already announced "great tax reform" as well as the tariff reductions and the simplification of import procedures to which the German government has already committed itself in a general way. But the committee realized that "the new effort requested of Germany is of a kind which meets with strong opposition in every country and will require, in some respects, a period of preparation."

The policies of expansion recommended both by the German Academic Council and by the OEEC Economic Committee are of course in accord with the balance-of-payments adjustment principle that a country in surplus may contribute to the adjustment by allowing her economy to expand, while deficit countries should follow the opposite policy. In the German case, if as a result of the recommended policy price rises were to occur, surpluses might tend to decline not only vis-à-vis the EPU area, but also vis-à-vis the dollar area, with which Germany has achieved balance only as a result of an unusually favorable set of political circumstances. Moreover, while Germany can be expected to allow a further expansion of her economy until all her economic resources, such as labor, are fully employed, it would not be healthy to recommend an expansion, over and above this, with an attendant price and cost rise, merely for the sake of enabling other countries to improve their trade position vis-à-vis Germany. Nor can Germany be expected to

[20] OEEC, *op. cit.*, p. 41.

carry the whole burden of adjustment; countries with balance-of-payments deficits may have to contribute their share. Any policies that she may decide to adopt would presumably be moderate, and consequently their effects would probably be unspectacular. Highly significant in this connection is the consideration that, as a result in particular of autarchy policies followed in the past, Germany's propensity to import is comparatively low (see Section I); and no sanguine expectations should therefore be attached to the recommended policies as regards the raising of the level of German imports.

In the longer run, greater balance in Germany's external accounts may be found by way of capital exports. It may be recalled that prior to the first world war, Germany, while importing capital on a short-term basis, was an exporter of long-term capital; German enterprises, for example, secured export orders by granting long-term credits, and in addition established foreign subsidiaries and branches.[21] However, with large domestic investment demands still to be met for such purposes as industrial rationalization and home construction, with high interest rates, and with the German capital market functioning poorly, Germany still has a long way to go before she would be in a position to replace the present automatic credit extensions to EPU and bilateral-clearing nations by genuine long-term capital exports. But certain conditions would in the longer run favor such a development: Germany, like the United States, is a large manufacturer of investment goods, and her industry has a considerable amount of know-how, both of which are substantial attributes of a country supplying capital exports.

Returning now to the more immediate future, Germany may be able to make further progress toward convertibility by liberalizing dollar imports to a higher degree and by eventually unfreezing all blocked assets. If she should be able to afford such policies, her situation would more and more approximate the Swiss pattern. Switzerland, like Germany, is a member of the EPU, and at the same time trades with a number of countries on a bilateral basis; apart from tariffs she maintains only minor quota restrictions vis-à-vis the dollar area. Foreign assets are of course not frozen, and the free outward flow of capital to all areas is authorized. However, vis-à-vis the EPU and bilateral countries, use of the Swiss franc is subject to the limitations involved in the multilateral or bilateral clearing mechanisms.

The Swiss "system," which can be characterized as full resident convertibility vis-à-vis all areas, and nonresident convertibility limited to residents of the dollar area, has the advantage that a country adopting it may simultaneously continue bilateral clearings with individual

[21] See, *Die deutsche Zahlungsbilanz,* Ausschuss zur Untersuchung der Erzeugungs und Absatzbedingungen der deutschen Wirtschaft (Berlin, 1930), p. 130.

countries and remain in the EPU, as long as this is deemed advantageous, and as long as the foreign contracting partners desire continuation of the clearing mechanisms. Germany appears to be primarily interested in resident convertibility; the Swiss system of full resident convertibility, if Germany could afford it, would allow her to free her economy from a large measure of bureaucratic controls, to buy in the cheapest markets, and possibly to attract new foreign capital.

As regards British plans for introducing nonresident convertibility, German financial authorities have rather unanimously expressed concern that Britain, in the effort to achieve nonresident convertibility, may push trade liberalization less vigorously and even raise restrictions on imports. Other Continental European nations have expressed similar reservations, but Britain has given repeatedly assurances that she does not expect to sacrifice trade liberalization to making sterling convertible to nonresidents. Significant in this connection is the official joint communique issued after the British-German financial discussions in early May, which stated that convertibility should not be considered "an end in inself but as a means toward securing a higher and more stable level of world trade." In any event, Germany, instead of pushing "financial convertibility," places special emphasis on the freeing of trade from quota restrictions—*i.e.*, on "commercial convertibility." She aims at such convertibility not only as applied by herself (resident convertibility) but also as applied by other nations, in order to raise her exports, especially to the sterling area with which she is running a deficit. She has been pressing for greater trade liberalization, particularly by those European trading partners that maintain lower liberalization ratios than herself, such as Britian and France.

Moreover, as regards nonresident convertibility, she can presumably be interested in such a scheme only if it embraces most of the present EPU nations. In fact, Germany is more interested in the convertibility moves that European countries *other* than Britain may make, as is indicated by the fact that in 1953 she has had a surplus on trade account with EPU countries other than the sterling area equivalent to $668 million but with the sterling area a deficit of $134 million. If the countries with which Germany is running surpluses could join in a British convertibility move, she would be well off. Germany not only could pay dollars to the United Kingdom for her sterling area deficit but in addition could earn a substantial net amount of dollars as a result of her over-all surplus position. She might even earn larger amounts of dollars than at present, since her EPU surpluses are now being settled only half in dollars, while under a full convertibility scheme these would be fully convertible into dollars.

But all this is highly conjectural and uncertain. As regards countries other than the sterling area, Germany in 1953 ran merchandise trade surpluses aggregating $336 million with countries that are fairly strong (Austria, Belgium-Luxembourg, the Netherlands, Portugal, Sweden, and Switzerland); and surpluses aggregating $332 million with countries that may be considered rather weak (Denmark, France, Greece, Italy, Norway, and Turkey). However, some of the less strong countries, with which, on the aggregate, Germany has also been running large trade surpluses, might not be able to participate in a British convertibility move, and might have to revert to bilateral clearings unless some form of a "rump" EPU were maintained. Therefore, the whole pattern of intra-European trade may well change.

The foreign trade of the weaker EPU countries, particularly with Germany, has been bolstered by the credits extended to them by the EPU, the chief burden of which Germany may be said to have borne; they may therefore be relied upon to oppose strongly a premature dismantling of the EPU mechanism and its replacement by full nonresident convertibility, which of course would not provide for the extension of credit. Similarly, Germany appears to take the position that plans for introducing nonresident convertibility could and should be implemented only when certain conditions have been met to avert the danger of any consequent shrinkage of trade. Among these conditions, the following would appear to be the major ones: (1) most European nations must be ready to join in such a move; (2) the convertibility plans must include provisions for the maintenance or further enlargement of the currently achieved degrees of trade liberalization; and (3) the weaker nations must be supported by lines of credit in place of the present credit extensions by the EPU. It can be said with confidence that Germany will lend its wholehearted cooperation in helping to meet these requirements, and will join in a concerted convertibility move if they are basically met.