L.5.2
CONFIDENTIAL

RFD. 49

swL

Board of Governors of the Federal Reserve System
Division of Research and Statistics
International Sections

REVIEW OF FOREIGN DEVELOPMENTS

December 2, 1946

....

The Danish Dilemma

Robert W. Bean

Despite her great good fortune in having come through the war almost unscathed, and in having been the only liberated country in Europe able to export more in 1945 than she received from abroad, Denmark's international economic position throughout 1946 has steadily worsened. The cows, pigs, and chickens which pay much of Denmark's way in the world have produced somewhat more than last year, but have not been able to prevent the mounting accumulation of debit balances in foreign trade, particularly with the country which has traditionally been Denmark's best market for butter, bacon, and eggs. This has come as a rude shock to the Danes, who have watched a credit balance with Great Britain, amounting at the end of 1945 to the equivalent of some 40 million dollars, turn into a debit balance of 140 million dollars. Nor has the prospect of continuing as unwilling lenders been pleasing to the British, who have now demanded that the Danes find a way to reduce the debit balance. Negotiations began in London during September, were resumed there early in November, and are expected soon to be taken up again in Copenhagen. The length of these negotiations, and the long recesses during which the Danish delegates have returned to confer with their Government, indicate the difficulty of finding a solution to the problem. As might be expected, the British urge that the Danes reduce their debit balance by exporting greater quantities of foodstuffs to Great Britain, whereas the Danes seek to obtain higher prices for their exports.

Essentially this problem is the result of the Danish Government's exchange rate policy adopted at the time of liberation. Denmark is the only liberated country in Western Europe which has not reduced the exchange value of her currency from the pre-war rates, despite the fact that even before the war she was encountering difficulties in her foreign trade balance owing to an internal rise of prices and wages, and despite a greater increase of internal prices during the war than occurred in her principal market and in competing countries. The German occupation authorities, who financed themselves out of the Danish National Bank, paid high prices for Danish butter, bacon, and eggs. At the nominal rate of exchange prevailing at the time of liberation, these prices were much too high for the British market. Instead of devaluing the krone, however, the Danish Government announced in July 1945 that, until a price agreement was reached with Great Britain, it would guarantee the maintenance of "German" prices for butter, bacon, and eggs exported to that country.

Agreement was reached in August 1945, but did not put an end to the need for Danish subsidy payments. Rather, the high sterling value of the krone was formalized, the prices paid by Britain for Danish foodstuffs were lowered by 10 per cent, and it was stipulated that by the end of 1946 prices paid to Denmark should be no higher than those paid to the Dominions. The Danes agreed to accept lower prices on the assumption that imports of feedstuffs would bring down their costs of production.

This expectation has not been realized. The quantity of feedstuffs obtainable has been disappointing, and the prices of most imports have been higher than was foreseen. In conformity with the agreement, however, an effort was made to lower the prices charged the British. Thus, the average price per pound of butter exported to Great Britain was reduced from 43 cents in November 1945 to 34 cents by June 1946, which was only partly a seasonal movement. Danish producers complained that this price was insufficient to cover costs. In July the Danes asked for new terms and, after several weeks of negotiations, the British agreed to pay higher prices (e.g., 40 cents per pound for butter) in return for guaranteed delivery of most of the Danish export surplus of foodstuffs. The higher prices paid by the British were still insufficient to satisfy the Danish producers, and in August the Danish Government increased its subsidies. The problem of covering production costs has now, for the time being, been met. The Danish producer receives about 45 cents per pound for butter which is sold to British housewives at 30 cents per pound, the difference (plus the cost of transportation and marketing) being made up by the Danish and British Governments. But the problem of covering the cost of Denmark's imports from Great Britain remains.

There are two possible solutions, neither of which appears attractive to both parties. The British consumer or the British Government might pay still more for Danish food products. Or Denmark might find a way to export a greater share of her total production to Great Britain. A third solution which would be satisfactory to both parties--an increase of production--appears not to be possible for the present, owing to the difficulty of obtaining animal feedstuffs.

Although the British have resisted further price increases, there may well be some concessions in the new agreement when it is reached. The British argue that they pay less to the Dominions for butter and bacon than to Denmark. Thus, under the agreement signed last July, Britain pays 39 cents per pound for Danish butter, compared with 31 cents per pound for New Zealand butter. But these prices are f.o.b. the producing countries, and the price differential in Britain is therefore somewhat less. Moreover, according to some reports the United Kingdom makes block payments to the Dominions to compensate them for low prices charged on animal product exports to the United Kingdom. Finally, the Danes claim that the prices which they must pay for imports have risen more since before the war than have prices received for their exports.

Whatever price increases are granted, however, they will not be sufficient to bring about a balance in Denmark's trade with Britain, and this course is therefore only a partial solution. This is readily apparent from the trade figures:

Table I
Denmark's Trade with Great Britain, January-September 1946
(In millions of dollars)

Month	Imports	Exports			Import surplus
		Total	Butter, bacon, and eggs	Other	
January	10	7	5	2	3
February	13	6	3	3	7
March	17	5	3	2	12
April	16	8	5	3	8
May	19	8	6	2	11
June	20	14	10	4	6
July	25	15	12	3	10
August	32	10	8	1	22
September	30	9	6	3	21
	181	82	60	22	99

A further price increase for butter, bacon, and eggs, of the magnitude granted last July by the British--roughly 20 per cent--would have reduced the trade deficit with Britain in September only from 21 to 20 million dollars. Since Denmark's export surplus to Britain in normal times is her means of financing an import surplus from other countries, it is essential that the value of exports to Britain should not only be brought up to, but should exceed, the value of imports.

The British are, therefore, right in insisting that Denmark must increase the volume of her exports and that, greater production being impossible for the present, this must be accomplished by cutting down domestic food consumption. To this proposal the Danes object that food rationing is difficult to enforce in a farming country. In arguing thus, they appear to ignore the effectiveness of a strong price incentive. Actually, the Danes cannot be unaware that a larger return in kroner would spur deliveries, but they are unwilling to provide this price incentive either by devaluation or by increased subsidies.

Since the conclusion of the July 1946 agreement with Great Britain, the marketing of agricultural produce in Denmark has been in the hands of the State. Products are delivered to the Government, which pays a fixed uniform price to the farmer. The Government determines the volume to be sold on the domestic market, and exports the remainder. Although prices obtained in the domestic and foreign markets differ (for example, the wholesale price of butter in Denmark is 42 cents per pound, but the British Government pays only 40 cents), the Danish producer receives the same amount in kroner whatever the ultimate destination of the products he delivers. Theoretically, under this system, it should be possible for the Government to allot a greater proportion of deliveries to the foreign market. In fact, however, they claim that official rations of foodstuffs already are at low levels, that much is consumed on the farms or sold through unofficial channels at higher prices, and that this drain on deliveries to the Government has placed a limit on the amount available for export.

The answer to this situation, in the absence of a program which would bring down costs and prices generally in Denmark, is to offer a higher price to farmers. This could be accomplished by increasing subsidies or by devaluing the krone. The effect this would have in expanding exports is indicated by the fact that, whereas in the years 1936-38 more than four-fifths of total butter production was exported, less than two-fifths was exported during January-April 1946. The supply of agricultural goods for export is elastic at present in Denmark, not because production can be increased, but because domestic consumption is on a relatively high level.

Not even the doubling of foodstuff exports to Great Britain, however, would suffice to eliminate the current trade deficit. Together with moderate increases in sterling prices, the effect might be to reduce the monthly deficit in trade with Great Britain by one-third. Clearly, therefore, attention must also be focused on Denmark's imports from Great Britain. Either import controls or devaluation of the krone might be used to reduce their volume.

It is this choice--between devaluation and the increased use of export subsidies and import controls--which presents a dilemma to the Danes. It is a choice which is more real for Denmark than for a number of liberated countries which could not hope immediately to better their balance of payments position by currency devaluation. If the Danes choose devaluation, the krone prices of all imports will be increased, they will run the risk of inviting new wage demands from the labor unions, and their foreign indebtedness will be magnified in terms of the quantity of goods which must be exported to service and repay it. If they choose increased export subsidies and import controls, they retain the advantage of being able to limit imports selectively, but aggravate their internal financing problems and keep in force a system which has been highly unpopular with the Danish farmers.

The likelihood that devaluation will force new wage increases is probably less in Denmark than in most liberated countries, because the principal item in the cost of living--food--is largely produced at home. Norway, despite having lowered the dollar value of her currency by 14 per cent, has succeeded remarkably well in keeping down money wages since liberation. Of the Western European countries engaged in or engulfed by the war, only Denmark has drawn back from exchange devaluation: the pound sterling and Norwegian krone have both been reduced by 14 per cent below their August 1939 value in Danish kroner, the Netherlands guilder by 29 per cent, the Belgian franc by 33 per cent, and the French franc by 68 per cent. Only the Swedish krona has appreciated (by 16 per cent) in terms of Danish currency. Undoubtedly the Swedish action has been a deterrent to the Danes, who received from Sweden 7 per cent of their total imports during the first three quarters of 1946, but their relations with Sweden can hardly be the deciding factor.

There is, finally, the possibility that Denmark might secure foreign credits which would enable her to continue the present trade deficits for a time.1/ She has applied for a loan of 50 million dollars from the International Bank. Her current deficit with all countries, however, is running at the rate of 30 million dollars per month (average for third quarter of 1946), so that it is difficult to avoid the impression that there exists a disequilibrium more serious than one which might be overcome by means of additional stop-gap credits.

1/ The London Financial Times (November 6, 1946) has even suggested that Denmark's existing debit balance with Great Britain might be reduced "from the proceeds of a loan from the International Bank, for which Denmark is already understood to have applied", but this can scarcely be taken as a serious suggestion.

The Philippine Balance of Payments and Economic Recovery

John Exter

Perhaps the most important problem facing the new Government of the Philippines is the reconstruction of the war-torn economy. The devastation in the Islands has been estimated at approximately one billion dollars in pre-war values, or roughly 1.5 billion at replacement cost. For a country whose total pre-war national income was estimated at about 700 million dollars the task of rebuilding seems almost insurmountable.

The outlook appears more hopeful, however, with respect to the Philippine balance-of-payments position over the next few years. At least through 1948 receipts promise to be large enough to permit a volume of imports of as much as 400 or 450 million dollars a year. The latter figure is three times the pre-war value of imports and 50 per cent greater than the annual rate during the first nine months of 1946. Even after 1948, receipts are expected to remain high enough to support imports very substantially above the pre-war level. It should, of course, be noted that, if present American prices are assumed to continue, the value of imports must be roughly 60 per cent greater than pre-war in order to represent the same physical quantity of goods.

The Philippine balance of payments is dominated by three principal items: on the receipts side, exports and United States Government payments; and on the payments side, imports. Of the exports, sugar and gold were most important before the war, accounting for about 55 per cent of the total in 1940. Sugar export is not expected to begin until 1948 and the recovery of gold mining is very uncertain. Nevertheless, the value of exports is rapidly approaching pre-war levels, primarily because of the high prices currently being paid for copra and abaca.

United States Government payments will be the most important source of receipts over the next two or three years. War Department and Veterans Administration expenditures are expected to predominate at first, with expenditures under the Rehabilitation Act later on assuming a larger role.

The War Department expenditures are due partly to the fact that back pay is owed the Army of the Philippines, which was incorporated into the United States Army in 1941 and of which recognized units continued to fight throughout the Japanese occupation. In addition, the War Department is building military installations in the Islands and still maintains an American troop establishment. Veterans Administration payments consist of pensions and death benefits under National Service Life Insurance policies.

Although the total volume of War Department and Veterans Administration payments is unknown, they will probably be large enough during the next two years to raise the total of United States Government payments to more than 300 million dollars a year. This is likely to be twice as much as the Philippines will be able to earn from exports.

In addition, the United States Congress in the Rehabilitation Act1/ has authorized appropriations for reconstruction purposes totaling 525 million dollars plus the transfer of surplus property located in the Islands having an estimated fair value of 100 million dollars. In passing this Act, Congress was recognizing an American obligation to help rebuild the Philippines which, with Pearl Harbor, were the principal American territorial possessions to suffer the destruction of war.

Although the Rehabilitation Act is generous, reconstruction thus far has been slow. Title I of the Act, providing for private claims, will be particularly hard to implement. Since the Philippine War Damage Commission is certain that its 400 million dollar authorization is inadequate to satisfy all claims, it will be reluctant to make large payments even on approved claims until all claims have been filed, which will probably be more than a year hence. The Act permits immediate and full payment of approved claims up to 500 dollars. The effect of such a procedure is to treat the smaller claimants more favorably than the larger. This has the disadvantage of delaying the rebuilding of the larger enterprises upon which depends the restoration of the productivity of the economy.

While the Philippines can thus look forward to a substantial inward flow of dollars over the next few years, they also have comparatively large balances already in the bank. At the end of August short-term assets in the United States totaled 466 million dollars, of which almost 400 million dollars was official. Of course, most of the official balances are tied up as currency reserves and therefore cannot be respent by the Philippine Government. They could be released in whole or in part for further monetary expansion either by abandoning the 100 per cent reserve requirement or by

---

1/ See Review of Foreign Developments, April 22, 1946.

a devaluation of the exchange rate. Presumably neither of these steps would be undertaken lightly. The 100 per cent reserve system is unlikely to be changed unless as a part of a comprehensive reorganization of the monetary system, which might well include the establishment of a central bank. And, according to a recent executive agreement with the United States concluded under the terms of the Philippine Trade Act, the exchange value of the peso cannot be changed except with the approval of the President of the United States. On the other hand, the currency reserves are freely available for financing temporary balance-of-payments deficits in so far as such deficits are accompanied, as they tend to be, by disappearance of currency from circulation.

Although the Philippines are in the extremely fortunate position of having adequate foreign exchange assets which may be expected to show a further growth during a period when the economy is prostrate, there remains a difficult problem of mobilizing available exchange to uses which are most essential to the rehabilitation and development of the economy.

The Philippines have no exchange controls, no duties on American goods (which now comprise about 95 per cent of total imports), and no system of import quotas or controls. At the same time purchasing power is more widely distributed than ever before, so that the funds in the hands of the poorer classes of the population are relatively large. These people prefer to improve their scale of living rather than to save and invest. The result is that, for a country whose primary task should be reconstruction, imports of consumption goods have been abnormally high and imports of capital goods disappointingly low. It may be expected that in the future, as the most urgent consumer wants are satisfied, as capital goods in the United States become more available, and as claims are paid by the War Damage Commission, the proportion of consumer to capital goods will decline. Even so, without any controls it is too much to expect that it will decline to the point where the country's long-run interests will best be served.

Unfortunately the Government is in no position at the present time to import capital goods on its own account. It inherited a tax system from the Commonwealth era which is totally inadequate to meet present revenue requirements. Nor are its prospects for internal borrowing very favorable. The Philippine public is not accustomed to investing its savings in government bonds and, without a central bank, the possibilities of sale of securities to the banking system are limited.

The United States left a legacy of laissez-faire to the Philippine economy. The exchange standard monetary system with its requirement of a 100 per cent reserve, mostly held in dollars, operates about as automatically as any system could in the modern world. Currency is still the dominant part of the money supply; and there is no possibility of monetary control without a central bank. The tax system is extremely light in its burden upon enterprise and initiative. There are few legal restrictions to the exploitation of the natural resources of the country. And, as already mentioned, there is complete freedom of movement for merchandise and funds between the Philippines and the United States, or, for that matter, most of the rest of the world.

It seems clear that, if the Philippine Government does nothing in the present circumstances, the reconstruction and development of the economy will be seriously retarded. Foreign exchange resources which are dissipated on luxury consumers goods during the next few years can never be recaptured. The core of the problem, then, is to mobilize the optimum amount of foreign exchange and domestic resources for rehabilitation without at the same time creating uncontrollable inflationary pressures.

Three principal approaches to the problem are likely to be considered sooner or later:

(1) The first is the imposition of import controls.[1] Such a system might exclude luxury goods altogether and severely curtail the import of semi-luxuries. Foreign exchange available for the purchase of capital goods would be correspondingly increased and could, if desired, be used over a greater number of years. To the extent that the system reduced the total volume of imports in any period, it would create inflationary pressures in domestic markets, but as long as real necessities were allowed to come in freely, it should be possible to hold down the basic cost of living as well as wage rates. At the same time, many persons might be induced to invest their excess purchasing power in government bonds.

(2) The second approach is a determined drive to increase government receipts, both through a drastic revision of the tax structure and a program of internal borrowing. Tax rates have already been increased, but early indications show that still higher rates and additional sources of tax revenue will be necessary. The prospects for successful internal borrowing should be more favorable than ever before because of the relatively large money supply and the unavailability of goods.

(3) The third approach, which has already been initiated by the Government, is to provide a mechanism for injecting investment funds into the economy. Legislation has been passed providing for the Rehabilitation Finance Corporation, a Philippine R.F.C., the capital of which is to be derived from the profits of sales of surplus property, and from excess monetary reserves resulting from the loss and destruction of currency in circulation. The Philippine R.F.C. is designed to provide such loan capital to businesses and governments as cannot be provided with reasonable risk by banks and other private lending institutions.

To the extent that the tax and internal borrowing program envisaged under (2) above is insufficient to balance the budget, the Government will be forced either to seek external loans or to create funds by relaxing the present rigid monetary reserve requirements. President Roxas has already proposed to the United States a five-year program of budgetary loans totaling 400 million dollars. The last American Congress authorized the Reconstruction Finance Corporation to lend 75 million dollars to the Philippines during fiscal 1947, and agreement on a first installment of 25 million dollars was announced by the R.F.C. on November 26. While external loans to meet domestic budgetary deficits may be justifiable as

---

1/ While the Philippine Trade Act permits exchange controls only with the approval of the President, import controls are not specifically prohibited.

a last resort, they may have an effect of diverting the attention of the Philippine Government from the important problem of preventing internal inflation and curtailing unnecessary imports. In particular, the pesos issued against the borrowed dollars, when spent by the Government to meet its internal budget needs, could be respent by the recipients on imported luxury goods. To the extent that this happens, the foreign exchange provided by the loan is dissipated without increasing either the productivity of the economy or the capacity to repay.

In conclusion, it should be noted that proper financial policies will do no more than provide a favorable environment for the revival of production in the economy. To increase real output it will be necessary to solve such immediate problems as relieving port congestion in Manila, breaking bottlenecks in the construction industry, and improving transportation. These and other tasks will tax to the limit the administrative capacities of the new Government.

Mexican Domestic Monetary Policies

David L. Grove

The monetary measures adopted by the Bank of Mexico during the war and the present post-war period may be divided into four broad categories:

(1) Quantitative controls over the total volume of bank credit, effected by raising reserve requirements and by establishing portfolio ceilings;

(2) Selective controls of bank credit, operating through greater vigilance over the destination of credit and through measures designed to encourage banks to shift from commercial loans to production loans;

(3) The sale of gold coin to the public for hoarding;

(4) Purchases and sales of securities, particularly Government securities.

1. Quantitative Controls

A. Reserve requirements. The Bank of Mexico has gradually raised the reserve requirements against sight and time deposits to 50 per cent for banks located in the Federal District or in places where the Bank of Mexico has a branch and to 45 per cent for banks located in places where the Bank of Mexico does not have a branch. Prior to the series of increases which began in 1942, reserve requirements were only 15 per cent for banks in the Mexican states and 20 per cent for banks in the Federal District. Reserve requirements against savings deposits have remained at 10 per cent.

B. Portfolio ceilings. The Bank of Mexico soon came to the conclusion that the increase in reserve requirements was failing to stop the rapid expansion in bank credit and that more credit measures of control were needed. In November of 1942, the Bank of Mexico persuaded the banks in the Federal District to agree to limit their portfolio to the level existing on October 31, 1942. In order that the banks might accomodate approaching seasonal needs, however, it was agreed that the limit would not enter into force until March 1, 1943, by which date the banks were to have reduced their portfolios to the level of October 31, 1942.

Some of the banks succeeded in evading this restriction by transferring funds to banks in the Mexican states to invest, since banks outside the Federal District were not subject to the portfolio limit. The Bank of Mexico endeavored to halt this evasion by a further increase in reserve requirements. At the end of 1943, however, the Bank decided to abandon the system of portfolio ceilings and to replace it by still another sharp increase in reserve requirements.

In spite of these drastic increases in reserve requirements, bank credit continued to expand. Accordingly, on May 22, 1944, portfolio ceilings were established once more. The banks agreed that any resources obtained as a result of increases in their liabilities above the level existing on May 17, 1944, would be maintained in the form of deposits in the Bank of Mexico or would be invested in gold, dollar balances, Government bonds, or in credit documents arising from agricultural operations endorsed by the Bank of Mexico. At the same time, the agreement also stipulated that investments in private securities would not exceed the figure reached in May, except at the cost of a reduction in the portfolio of the bank. Thus, the re-adoption of portfolio ceilings was made, to a limited extent, to serve purposes of selective as well as general credit control.

In 1945, as a result of increasing pressure from the banks, the Bank of Mexico authorized the banks: (1) to expand their portfolios by an amount equal to 10 per cent of the level existing on May 22, 1944; (2) to invest an equivalent amount in private securities; and (3) to invest 10 per cent of their reserve deposits in Government securities. This last provision gave the banks an opportunity to earn a return on funds that would otherwise have had to be held as idle reserves. A minimum portfolio ceiling of 5 million pesos was also established.

2. Selective Controls

A. Rediscount rates. Because of their large excess reserves, recourse to central bank credit has been unnecessary for most banks. The rediscount policy of the Bank of Mexico has been oriented much less toward restricting the total volume of bank credit than toward encouraging production loans. In 1942, the Bank established as a prerequisite to the use of its rediscount facilities that a bank have at least 60 per cent of its portfolio in the form of production loans. Moreover, the rediscount rate on production loans was reduced to a par with that applicable to commercial loans (i.e., 4-1/2 per cent) and the rate for agricultural loans was later reduced still further to 3 per cent. This preferential rate for agricultural loans had little effect because the banks rarely found it necessary to borrow from the central bank. The National Bank of Foreign Trade did, however, borrow substantial amounts from the Bank of Mexico in order to finance agricultural operations and to facilitate the importation of essential goods as part of the Government's program to check rising prices.

B. Other selective measures. In 1943, in order to stimulate agricultural loans, the Government established and entrusted to the Bank of Mexico a National Fund to Guarantee Agricultural Credit Operations. The Fund contained 5 million pesos. Its purpose was to absorb part of any losses which banks might incur in their agricultural loans. The amount of loans made with the guarantee of this Fund, however, was very small.

Another measure of selective control was designed to check the rise in prices of urban real estate and to prevent capitalization and insurance companies from encroaching on the operations of the mortgage banks. This measure took the form of an agreement on the part of these companies, in 1944, to limit their mortgage loans to existing levels.

3. Sale of Gold Coin to the Public

One of the anti-inflationary measures adopted by the Bank of Mexico has been the sale of gold coin to the public for hoarding. The Bank has reported that from 1941 to the end of 1945 a total of 378 million pesos of gold coin, equivalent to 78 million dollars, were sold. It is believed, however, that a considerable part of the gold sold has been illegally exported rather than hoarded.

4. Purchases and Sales of Securities

The anti-inflationary measures adopted by the Bank of Mexico have, to a great extent, been nullified by its purchases of Government securities made necessary by the fact that the Mexican public has proved unwilling to purchase more than a limited amount of such securities. The Bank has been aware of the undesirability of monetizing the national debt but the financial needs of the Government for its programs of public works, national defense and economic development have prevailed. The Bank of Mexico has also engaged in open-market operations for purposes of stabilizing the Government bond market.

In addition to its purchases of Government securities, the Bank has also purchased bonds which the "financieras" have issued against industrial and agricultural paper, to help these institutions to develop long-term industrial credit. In order to provide an incentive to the "financieras" to place their bonds with the public, however, the Bank established as a prerequisite to its purchase of such securities a return of one-fourth per cent above the nominal yield. It has been reported that the Bank has now ceased buying the bonds of these institutions.

5. Concluding Comments

The money supply in Mexico increased from 919 million pesos at the end of 1939 to 4,184 million at the end of April 1946, an increase of 355 per cent. In spite of the anti-inflationary measures taken by the Bank of Mexico, nearly half of the increase in the money supply had its origin in bank credit expansion, both by the Bank of Mexico and by the other banks. In the case of the Bank of Mexico, purchases of Government securities played by far the leading role; in the case of the other banks, purchases of Government securities were small as compared with the expansion of loans. The increase in bank credit would undoubtedly have been still greater, however, had it not been for the measures adopted. The other half of the increase in the money supply is attributable almost entirely to the monetization of the large surpluses in the balance of payments. A very small part of the increase may be traced to the purchases by the banks of domestically produced silver and gold.

The conservative credit policy of the Bank of Mexico has been subjected to considerable attack. Opponents of the policy argue that many of the new enterprises created during the war are still in the process of construction and need funds for completion. Many other new enterprises are just beginning operations and badly need working capital. The proponents of these arguments assert that the tight money policy of the Bank of Mexico will strangle enterprises which are basically sound and desirable. It is further stated that the restrictive credit policy has maintained interest rates at exorbitantly high levels. On the other hand, it is clear that the conservative policies of the Bank of Mexico have placed the banks in a highly liquid and relatively strong position which should, at least in the long run, have a highly beneficial effect on Mexican economic progress.

Note on the Structure of Industry in Russia

Alexander Gerschenkron

Russian statistics regarding pre-war Five Year Plans regularly disclosed the relation between the aggregate output of producers' goods and that of consumers' goods. The current (Fourth) Five Year Plan furnishes this information neither for 1945 nor for any of the years of the plan period 1946-1950. The following tabulation, inadequate and incomplete as it is, may shed some light on how the structure of Russian industry contemplated for the last year of the present Plan compares with that of a pre-war year. For the latter, 1937 was chosen as the last peace-time year when military expenditures were still fairly low. Comparison is also made with the structure of industry indicated for 1942 in the original projection of the Third Five Year Plan.

Output of Selected Industrial Commodities1/

Industry	1937	1942 2/	1950 2/	1950 as of 1937	1942 as of 1937	1950 as of 1942
Producers' Goods:						
Pig iron	14.5	22.0	19.5	134.5	151.7	88.6
Steel	17.7	28.0	25.4	143.5	158.2	90.7
Rolled steel	13.0	21.0	17.8	136.9	161.5	84.8
Coal	127.3	230.0	250.0	196.4	180.7	108.7
Oil	30.5	54.0	35.4	116.1	177.0	65.6
Electric power	36.4	75.0	82.4	226.4	206.0	109.9
Locomotives	1,581.0	2,090.0	2,200.0	139.4	132.2	105.3
Freight cars (two-axle equivalent)	58.8	90.0	146.0	248.3	153.1	162.2
Metal-cutting machine tools	36.0	70.0	74.0	205.6	194.4	105.7
Merchant timber hauled	111.3	200.0	280.0	251.5	180.0	140.0
Consumers' Goods:						
Cotton fabrics	3,442.0	4,900.0	4,686.0	136.0	142.4	95.6
Woolen fabrics	105.0	175.0	159.0	151.4	166.7	90.9
Sugar	2.4	3.5	2.4	100.0	145.8	68.6
Leather footwear	164.2	235.0	240.0	146.1	143.2	102.0

1/ The units of measurement are as follows: pig iron, steel, rolled steel, coal, oil, sugar - millions of metric tons; electric power - billions of kilowatt hours; locomotives - units; freight cars and machine tools - thousands of units; timber - millions of cubic meters; textiles - millions of meters; footwear - millions of pairs.

2/ Plan.

A few tentative conclusions may be based on these data:

(1) By 1950 output of a number of specific products of the first group (coal, electric power, freight cars, metal-cutting machine tools, and merchant timber) is to increase much more, in relation to 1937, than the output of any of the four important consumers' goods listed. On the other hand (excepting the special case of oil), the proposed output of the remaining producers' goods (pig iron, steel, rolled steel, locomotives) stands in about the same relationship to 1937 production as does that of the consumers' goods listed. Small as this range of commodities is, it indicates that the relative weight of producers' goods in Russian industry is scheduled to increase in comparison with 1937. This will not result exclusively from adjustments taking place in the period 1946-1950, for production during the war undoubtedly increased the share of heavy industry in the aggregate industrial output. M. Voznesenski, however, in his speech to the Supreme Soviet of the U.S.S.R., stated that "the rate of growth of output of means of production will somewhat exceed the rate of growth of output of consumption goods."

(2) On the other hand, it will be noted from the last column of the preceding table that with certain exceptions the structure of output scheduled for 1942 and that now scheduled for 1950 is not too different.

In the producers' goods category (again disregarding oil) only freight car production and merchant timber are considerably in excess of the levels planned for 1942. Among the consumers' goods, only the sugar production for 1950 is scheduled to be far below the projection for 1942. For the remaining commodities shown the ratio of 1950 to 1942 production is rather close to 100. In other words, the 1950 Plan may on the whole contemplate a relation between output of producers' and consumers' goods which is rather similar to that of the Third Five Year Plan. The ratios for 1937 and 1942 are as follows:

Industrial Production

	1937	1942	1937	1942
	(In billions of 1926/27 Rubles)		(Per cent)	(Per cent)
Means of production	55.2	112.0	57.8	62.2
Consumers' goods	40.3	68.0	42.2	37.8
			100.0	100.0

That a considerable increase in the share of producers' goods in total industrial output was planned between 1937 and 1942 is not surprising. Only a few months separated adoption of the Third Five Year Plan from the outbreak of World War II. The proposed structural shift was doubtless dictated by military considerations. Much as the Soviet leaders continue to stress such considerations at present, they seem reluctant to admit that the structure of industry proposed for five years after the end of the war will be the same as that on the eve of the conflict.

It is another question whether this structure will actually be achieved. The present Five Year Plan has been drawn up at a time when most problems left in the wake of the war are still unsolved. Successful settlement of these problems might induce the Russians to change their goals, and past experience has shown that Soviet economic plans are sufficiently flexible to be adapted to changing circumstances. More important in the short run, however, is the fact that economic reconstruction as a whole may be jeopardized unless more emphasis is placed on the output of consumers' goods. All evidence in recent months points to the grave effects which shortages of consumers' goods have had on the productivity of labor. The recent measures (Decree of November 9) concerning extension of the function of cooperatives and encouragement of additional production of consumers' goods by these organizations may be regarded as the first serious deviation from the structure of production originally proposed for Russian industry.