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REVIEW OF FOREIGN DEVELOPMENTS

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STABILIZATION IN URUGUAY

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The inflationary forces exerting an upward pressure on Uruguayan money incomes and prices in the postwar period appear to have been reduced greatly in intensity by the end of 1948. During the war itself, Uruguay experienced moderate price increases compared with other Latin American countries, the cost of living having risen about 1/3 between 1939 and 1945. In the two succeeding years, the cost of living rose by about 25 per cent, but since the fourth quarter of 1947 the index has been fairly stable.

The abrupt halt in the rise of the cost-of-living index which occurred in late 1947 can be attributed to the establishment of more rigorous controls over prices of essential goods, including the use of subsidies, as well as to an apparent stabilization of over-all demand. In August 1947, the Government established a new price-control and civilian-supply agency which has administered controls on the prices of many of the essential goods appearing in the cost-of-living index. Rentals have been rigidly controlled for several years, although a rent raise of 20 to 30 per cent was authorized by the Uruguayan Congress in October 1948. From August of 1947 to December of 1948 the food component of the cost-of-living index declined about 7 per cent. Although there is much evidence that the index reflects only official prices rather than prices prevailing in actual transactions,^{1/} the impression of greater

^{1/} The cost-of-living index for Uruguay applies only to the City of Montevideo and covers only the basic commodities and services purchased by workers' families. Thus, the living costs of families on higher income levels, who presumably would purchase more goods not under price controls, would be proportionately higher. In the case of rents particularly, it is reported that "bonus" payments are common.

price stability in 1948 displayed by the general index probably is valid. The recent success achieved in the use of direct controls and subsidies has been greatly facilitated by a stabilization of over-all demand. Although data do not exist to show the development of the various components of the gross national product since the end of the war, this stabilization may be inferred from the emergence since 1947 of (1) a surplus in the Government's budget, (2) a deficit in the balance of payments on current account, and in 1948 (3) a decline in the volume of domestic investments.

Budget and Public Debt

During the period 1941-46, inclusive, Uruguay experienced substantial budgetary deficits, with expenditures in 1943-45 about 40 per cent larger annually than receipts. In the postwar year however, budgetary receipts increased rapidly, the 1948 projected annual receipts of approximately 258 million pesos being almost double the returns for 1945. As can be seen from the following table, these budgetary trends resulted in slight surpluses for the years 1947-48.

	<u>Budget and Public Debt</u> (millions of pesos)				
	<u>Receipts</u>	<u>Expenditures</u>	<u>Domestic Debt</u>	<u>Foreign Debt</u>	<u>Total Debt Outstanding</u>
1941	95.2	114.8	336.2	140.7	476.9
1942	97.4	126.0	387.2	138.2	525.4
1943	94.5	138.9	425.1	135.9	561.0
1944	101.1	145.6	460.2	135.3	595.5
1945	130.2	170.4	507.7	133.7	641.3
1946	183.8	206.9	546.9	131.1	678.0
1947	240.8	231.8	579.5	128.6	708.1
1948	257.5 <u>1/</u>	248.1 <u>1/</u>	637.7 <u>2/</u>	122.5 <u>3/</u>	760.2 <u>4/</u>

1/ Annual rate projected from 11-month figure. Receipts adjusted for profits from exchange operations for only 10 months.

2/ It is assumed that the floating debt remained zero from October 31 through December 30; the total domestic debt is therefore shown equal to the long-term debt as of that date.

3/ The source of this figure is the "Deuda Publica Nacional". Data on the foreign debt for earlier years taken from this source do not apparently agree with the data shown above taken from the U. N. publication "Public Debt". For the years 1944 through 1947 the discrepancy ranges from 3.6 million to 4.3 million pesos. If the series continued to differ by similar magnitudes during 1948, the figure shown would appear to require an upward adjustment of about 4 million pesos to achieve comparability with data for previous years.

4/ This figure includes the unadjusted foreign debt. See footnote 3.

The principal sources of revenue are customs receipts and indirect taxes which together now yield somewhat more than half of total receipts. Since 1944 the excess profits tax has shown a marked increase as a source of revenue, both in absolute and relative terms. There is no income tax in effect in Uruguay and taxes on capital are reported to be quite moderate in order to encourage investment of foreign capital. With the exception of the excess profits tax, the tax structure is essentially regressive.

Little information is available on Government expenditures. Disbursements are reported in three broad categories: Budget, Public Works, and Treasury, but the distinction among them is not clear. It is reported that during 1948 attempts were made to reduce the outlays for Public Works. This may reflect the concern with which the Government has viewed growing inflationary pressures.

The total public debt of Uruguay has increased steadily during recent years, although the amount of the increase generally declined from year to year through the end of 1947; the rate of increase in the public debt during 1948 reversed this trend. The changes in total debt outstanding reflect the elimination of domestic short-term indebtedness and an orderly reduction of foreign indebtedness, both of which have been more than offset by substantial increases in domestic long-term indebtedness. Short-term domestic indebtedness which reached 32.3 million pesos in 1942 was extinguished by the end of 1947, partly through consolidation into long-term bond issues. As of October 31, 1948, no further short-term indebtedness had been incurred and on that date the Treasury was reported to have held a balance of 12.3 million pesos. The foreign debt, principally U. S. dollars and pound sterling, has been gradually reduced by about 10 per cent from the end of 1941 to the end of 1948, after adjustment is made for comparability with the remainder of the series. (See footnote 3, above table.) Domestic long-term indebtedness at the end of 1941, 308.8 million pesos, more than doubled by the end of 1948, when it amounted to 637.7 million pesos. About 28 per cent of this increase occurred since the end of 1946.

It is difficult to explain the paradox of continued growth of public debt during 1947-48 and the reported budgetary surpluses of those two years. In the previous years of deficit financing, the Uruguayan Government, while it did resort to central bank credit, relied primarily upon the financial resources of lenders other than the Banco de la Republica and the commercial banks. In fact, during the three-year period 1943-45 significant amounts of central bank loans and discounts to official entities were repaid, even though Government deficits were at their peak. Similarly, commercial bank investments in public debt bonds and treasury certificates were reduced each year during 1944-47. In 1947, however, Government borrowing from non-bank lenders dropped precipitously almost to zero while borrowing from the central bank increased substantially. Data for the first 11 months of 1948 reveal further Government borrowing from the central bank which approximates the 1947 rate. In view of the approximately 9 million peso surpluses reported for both 1947 and 1948 it is difficult to explain an increase in Government borrowing from the

central bank and the even greater increase in total public debt even if the growth of deposits of official entities and the purchases of certain public utilities formerly owned by the British are taken into account.^{1/} The price paid in late 1947 for the British-owned Montevideo Tramway, \$1.8 million, is equivalent to about 11 million pesos, only slightly more than the reported surplus. Even more difficult is the reconciliation of the substantial increase in the internal public debt during 1948. A possible explanation may be the advance raising of funds for the purchase of the remaining British-owned properties which Uruguay has contracted to purchase for \$43 million (\$10.4) or approximately 65 million pesos. It is expected that these transactions will be completed during the present year.

Balance of Payments

The Uruguayan economy is particularly sensitive to changes in its international transactions. Gross receipts in the balance of payments on current account rose by about 25 per cent between 1945 and 1947. As can be seen in the table below, this exerted an important inflationary impact on Uruguayan prices and incomes. Although imports of goods and services expanded even more than exports during this period, the deflationary impact of imports was offset in its initial stages by several factors. The expansion of imports was financed to a considerable extent by funds which had been accumulated during the war when imports were unavailable and when, as a consequence, their volume was low relative to an expanded national income. Later, however, as these funds were disposed of for the purchase of imported goods, an increasing portion of imports was financed by withdrawals from the current income stream.^{2/} Also the deflationary effect of the initial increase in imports was partly offset by an accumulation of business inventories of imported goods which, after 1947, probably levelled off. As the following table shows, the deficit on current account reached its maximum in 1947. Nevertheless, the 1948 deficit, though smaller than in 1947, probably exercised a greater deflationary impact than is apparent from a comparison of the two figures.

Domestic Investment.

During the early postwar period, there was a great expansion in domestic investment, including the accumulation of inventories. Construction constitutes a very important part of domestic capital formation in underdeveloped countries such as Uruguay. Data on building permits issued in Montevideo indicate an increase of about 43 per cent in the value of construction between 1945 and 1947. The shift during 1948, therefore, to smaller lower-priced building structures with a sizable decline in the value of construction, we may infer, has contributed to a stabilization of national income.

^{1/}It is rather justifiably assumed that such purchases are not included among the Government's budgetary expenditures.

^{2/}Revenues from customs duties and exchange profits magnified the deflationary impact of the rise in imports.

Data Relating to Income and Price Movements in Uruguay

1944-1948
(millions of pesos)

	Surplus or Deficit in Bal. of Pay- ments on Cur. Acct.	Budgetary Surplus or Deficit	Money Supply	National Income	Index of Value of Constr. in Montevideo 1944 =	Cost of Living Index 100
	(1)	(2)	(3)	(4)	(5)	(6)
1944	+ 39.5	- 44.5	284.7	637	100.0	100.0
1945	+ 47.1	- 40.2	320.9	632	152.2	114.5
1946	+ 17.6	- 23.1	406.1	941	169.1	126.3
1947	- 59.8	+ 9.0	390.8	993	217.5	145.5
1948	- 28.9	+ 9.4	399.9		172.2	146.7

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- (1) Through 1947 based on balance-of-payments data of Banco de la Republica; 1948 is a rough estimate. Data converted into pesos at 1,519 pesos per dollar.
 - (2) Based on data published by Ministry of Finance. Includes exchange profits, which are shown in the accounts of the Government for the year when exchange is actually sold; 1948 figure is estimate based on actual receipts for 11 months, excepting exchange profits for only 10 months.
 - (3) Defined as notes in the hands of the public and demand deposits of the public. Data are end-of-year figures excepting 1948 which is end of November.
 - (4) Estimates by Staff of International Monetary Fund.
 - (5) To permit comparison with data available for 1948, covers first 11 months of each year.
 - (6) Based on data published by Banco de la Republica and Ministry of Finance.

Monetary and Banking Situation

During the war, means of payments increased substantially. The increase was produced primarily by the monetization of the inflow of gold and foreign exchange, since the reduction in loans and investments of the Banco de la Republica ^{1/} more than offset the credit expansion of the commercial banks. Since 1945, however, the Banco de la Republica expanded its own credit operations. In 1946 credit expansion by the Banco and the commercial banks accentuated the inflationary impact of the gold and foreign exchange inflow. In 1947 the losses of gold and foreign exchange produced a decline in the means of payment, although credit expansion continued. During 1947, however, the velocity of turnover of bank deposits, as reflected in clearing house transactions, increased greatly. Since mid-1948 there is evidence of an abatement of inflationary forces, the money supply, particularly that portion held as demand deposits, having declined slightly but steadily through November, the latest date for which information is available. Nevertheless, credit expansion by the banking system continued in 1948, though at a slower rate than in 1947.

Since 1946 the monetary situation on balance does not reflect the presence of powerful inflationary forces. However, this is due principally to the deflationary impact of balance-of-payments deficits, and the movement of the money supply as such may not be very significant. The monetary authorities have taken few steps to tighten credit; during 1948 such moves were limited to half point increases in discount, loan, and commission rates charged by the banking system. On the other hand, interest rates on time and savings deposits have been reduced, a possible further indication of the stabilization of over-all demand and the decreasing opportunity for domestic investment.

Outlook

The present phase of the Uruguayan economy is characterized by an emergence of a surplus in the Government's budget, a deficit in the balance of payments on current account and a decline in the volume of domestic investment. The budgetary surplus and current account deficit together amounted to about 69 million pesos in 1947 and about 38 million in 1948. In a country where the national income is about 1 billion pesos, this constitutes a significant offset to domestic investment, which had itself apparently declined in 1948.

It is by no means clear, however, that inflationary forces have been brought under full control. As indicated above, price developments in 1948 may not be clearly reflected in the cost-of-living index. There are reports of an estimated 15 per cent increase in the cost of living from June 1948 to the end of the year, despite the relative stability of the official index. Lastly the conflicting data on government fiscal operations necessarily qualify any appraisal of Uruguay's domestic situation.

^{1/} The Banco de la Republica, though not possessing many of the attributes of a central bank, derives a powerful influence from the fact that it engages in extensive credit operations and holds the required reserves of the other banks.

While the general impression that a certain degree of stabilization has occurred is probably correct, there remain many factors which could result in a resumption of inflationary trends. The shift and decline in private construction activity which has occurred may be only temporary. Although urban land values and costs of construction have risen greatly, there remain many large projects, including hotels and office buildings, in the planning stage. Further expansion in bank credit would facilitate a resurgence of construction activity. In the field of government construction, the authorities appear to have been aware of the need to screen public works projects. A technical commission was formed in 1948 to examine all new public-works proposals before they are accepted by the state. There is, however, evidence of great need for larger outlays on roads and low-cost housing. It has been officially estimated that there are 120,000 sub-standard dwellings in Uruguay. During 1948 the policy of economy imposed by the national government was challenged by the Instituto Nacional de Viviendas Economicas, an advisory group on low-cost housing, which resigned in a body.

The Executive budget message of March 15, 1949, the first presented to the Uruguayan Congress in five years, and the additional projects which have been or are likely to be approved by the Congress call for expenditures exceeding estimated receipts by about 38 million pesos. The excess expenditures are to be financed by receipts from new taxes which are now being legislated, as well as by exchange control profits which are reported to have been omitted from the estimated receipts. If this is so the 1949 budget may well show a surplus rather than the deficit shown at present.

It is possible that the Uruguayan Government will tolerate a continuation of a deficit in its balance of payments on current account, though at a lower level than in 1948. If the Government should attempt to conserve its foreign exchange holdings by more vigorous controls on imports without at the same time imposing restraints upon internal demand, the Uruguayan economy may be subjected to more inflationary forces than have recently prevailed, particularly since a substantial reduction in imports would also greatly reduce Government receipts.

On balance, it would appear that the Uruguayan economy in 1949 will in general be stabilized in spite of the presence of some inflationary forces.

RECESSION IN BELGIUM

Robert Solomon

The Belgian economy began to show signs of a slackening in economic activity during 1948. This development manifested itself in a growing level of unemployment, especially toward the end of the year. Thus in November there were 174,000 wage and salary workers either completely or partially unemployed. By February of this year industrial unemployment had risen to 245,000 or almost 12 per cent of the total number of insured wage and salary workers in industry.

This development must be viewed in the light of Belgium's earlier postwar experience. Belgium emerged from the war in a more fortunate situation than its neighbors. The extent of war damage, though serious, was much less severe than in France and the Netherlands, and a relatively early and quick liberation enabled the industries of Belgium and Luxemburg ^{1/} to resume production more rapidly than other countries and to supply many of the products required by their neighbors' badly depleted economies. In addition, Belgium earned large amounts of gold and dollars soon after liberation as a result of the use of its ports by the allied armies and the expenditures of allied troops. Finally, Belgium's rich colony, the Congo, did not become a drain on the resources of the mother country; in fact foreign investments were not seriously impaired during the war period.

In addition to these more or less fortuitous factors responsible for Belgium's good fortune, mention must be made of the monetary reform which was carried out, under the direction of M. Gutt, shortly after liberation. The exchange of currency and blocking of deposits at that time enabled Belgium to remove direct controls fairly early without experiencing a serious inflation. Belgian policy in this regard was to encourage consumption, even at the expense of reconstruction, by using foreign exchange reserves to finance the importation of large quantities of consumer goods from the Western Hemisphere.

As a result of these circumstances and policies, the average standard of living in Belgium and Luxemburg was restored to prewar levels at a relatively early date. Moreover, as production and exports increased, the traditional trade surplus with other European countries reappeared. ^{2/} The relatively high degree of recovery is indicated by the "hardness" of the Belgian franc and the persistent tendency for European countries to exceed the credit margins in their commercial agreements with Belgium-Luxemburg.

^{1/} This paper is concerned mainly with internal developments in Belgium. However, the foreign trade statistics of the two countries are not separable and, in fact, the economies are closely related in an economic union. When Belgium's foreign trade is mentioned the data will refer to both countries. The discussion of internal developments will refer only to Belgium, although much of it is also applicable to Luxemburg.

^{2/} It may be noted that the distribution of that surplus has changed considerably since before the war. Whereas the United Kingdom was previously Belgium's largest debtor in merchandise trade, it is now a creditor in such transactions but this Belgian deficit is more than offset by earnings of sterling on invisible, and perhaps capital, account. In addition the Netherlands has become Belgium's largest debtor. In fact, aside from trade with the Netherlands, Belgium has been a net debtor in intra-European merchandise trade during 1947 and 1948.

Production and Employment in 1947 - 1948

It was during 1947 that industrial production attained the prewar level. During that year unemployment was at a relatively low level; where it did occur, special circumstances, — such as shortages of raw materials or, in the case of dock workers, the low level of transit trade due to Germany's economic stagnation — were responsible.

Along with the rising level of production, exports increased markedly. While prices continued to rise during the year it would appear that the rising world price level and the removal of subsidies were primarily responsible, rather than the pressure of internal demand. The fact that, toward the end of 1947 when many subsidies were removed, the rise in retail food prices was accompanied by a decline in retail prices of non-food products tends to bear out this observation.

It may be said that 1947 was a year of re-stocking for both consumers and producers in Belgium. The rising level of domestic production and the large-scale imports of consumer goods permitted Belgian families to purchase clothing, household furnishings, and other consumer goods of which they had been deprived during the war. Likewise industrial and commercial pipelines were refilled; in fact there undoubtedly was some speculative accumulation of inventories in anticipation of further price increases and rising production. Unfortunately on this as well as many other aspects of the Belgian economy, there is no adequate statistical information. 1/ It has been estimated, however, that increases in inventories in 1947 may have amounted to as much as 10 billion francs, or over one-half of net private investment. 2/

At the end of 1947 and continuing throughout 1948 unemployment began to increase, as may be seen in the following table.

<u>Unemployment in Belgium</u>			
(daily average of controlled unemployment in thousands)			
	Completely Unemployed	Partially Unemployed	Total Unemployed
1947 (mo. av.)	36	32	68
March	43	51	94
June	26	20	46
September	30	16	46
December	57	40	97
1948 (Jan.-Nov. mo. av.)	74	45	119
March	64	31	95
June	62	43	105
September	81	43	124
November	112	62	174
December	172*	80	252

*Abnormally swelled by strike of 60,000 "frontaliers" who cross the French border daily to work in French factories.

1/ Economic analysis is hampered by the absence of adequate and reliable statistical data concerning wages, inventories, consumption, investment, government finance, balance of payments and national income. As a result, hypotheses concerning developments in Belgium cannot be tested properly and must be considered as highly tentative.

2/ Belgium and Luxemburg - Country Study, Economic Cooperation Administration, Washington, D. C. Feb. 1949, p.12.

In spite of the growing unemployment, however, the general level of production did not decline. Whereas the industrial production index for the period January - November 1947 averaged 102 (1938 = 100, it was 111 for the same period of 1948.

If it were assumed that the size of the labor force did not change (the population of Belgium is almost constant) the average level of employment during the first 11 months of 1948 would have been about 3 per cent below that for the year 1947. Even if some allowance is made for an increase in the labor force as a result of re-entries during the year, the maintenance of a high level of production simultaneously with the emergence of large scale unemployment stands in need of explanation. In the first place productivity probably rose as a result of a steadier flow of raw materials, improved organization of production and installation of new equipment. Secondly, it is likely that a significant portion of the unemployment occurred in the distributive trades (both legal and black market) which had mushroomed in the early postwar period. Finally those industries in which production declined (e.g. textiles) use more labor per unit of product than those in which production continued to increase (e.g. iron and steel).

Unemployment rose almost steadily during 1948 while the index of production, except for seasonal variation, remained virtually unchanged at the level which had been reached during the fourth quarter of 1947. There were, however, declines in output in the textile and other consumer goods industries, which were offset by increasing production in the metal industries.

There also was evident, beginning around the middle of 1948, a slight decline in both the wholesale and retail price levels. This development has apparently continued to the present, after a slight interruption in the autumn: nevertheless, the extent of the decline is still hardly perceptible. For the year as a whole the average level of retail prices was about 15 per cent higher than in 1947.

Causes of Unemployment

It has frequently been said that the growth of unemployment is primarily caused by the "austerity" policies of other European countries which are restricting their imports of Belgian products. However, an examination of Belgian trade statistics does not provide support for this thesis. The total value of exports to Europe was about 17 per cent higher in 1948 than 1947. Moreover, during 1948 a slight upward trend is discernable, especially after September, when unemployment was growing rapidly.

It is also significant to note that exports to all areas were about 20 per cent higher in 1948 than in 1947 and that the rate of growth was greatest during the last half of the year. On the other hand, imports, which had reached a peak in the last quarter of 1947, declined sharply at the beginning of 1948 and varied little throughout the year, with the result that the total for 1948 was just about the same as for 1947. It is therefore evident from an examination of aggregate trade figures that the growth of unemployment and the tendency toward recession in Belgium cannot be ascribed to a contraction of exports.

Unfortunately, it is not possible from published statistics to make a commodity-by-commodity comparison of exports in 1947 with those in 1948, because of a change in customs classification on January 1, 1948. Two observations may be made, however, concerning the decline in textile exports, which has been cited most frequently in Belgium as being the cause of the growth in unemployment. According to the National Bank of Belgium, total exports of textile products had contracted only about 10 per cent in 1948 relative to 1947. 1/ Secondly, according to trade statistics for the year 1948, the value of textile exports were only about 2 per cent lower during the last quarter than during the first quarter of 1948. The index of production for the textile industry, on the other hand, was about 13 per cent lower.

The decline in the production of textiles and other consumer goods during 1948 must therefore be explained primarily by a contraction of internal demand. In this regard one possible explanation suggests itself from an examination of the retail price trends of food products compared with non-food products. With the progressive elimination of price controls, rationing and subsidies during the past two years, retail prices of food products have risen from an index of 281 (1936 - 38 = 100) during the first half of 1947 to 347 in December 1947, and an average of 384 for the year 1948. Although the actual retail costs to Belgian families may not have risen as much as these figures might indicate because they do not take account of black market prices in early 1947 when the latter were important, the fact remains that food prices have risen considerably. As a result expenditures on other consumer goods may have levelled off. This thesis tends to be substantiated by the observation that the non-food retail index was only about 2 per cent higher in 1948 than in 1947. In the absence of wage statistics for Belgium it is not possible to attempt a comparison of wages and prices. It may be noted, however, that, officially wages are still under control and wage increases require government authorization. Although this control has been gradually relaxed, it is quite possible that its success in preventing a wage-price spiral has had the effect of causing wages to lag behind prices sufficiently to cause a decline in consumer demand.

Another contributing cause to the growth of unemployment in Belgium may be a contraction in private investment. Deliveries of fabricated metal products to the internal market fell off after the first quarter of 1948, but it is not known whether this development is due to a decline in investment activity or in production of durable consumer goods. Although "voluntary" inventory accumulation has undoubtedly declined considerably and some stocks have been liquidated, it is likely that "involuntary" accumulation of inventories of finished consumer goods has occurred, and has, in turn, led to a falling off in new orders and production.

As was mentioned earlier exports increased markedly in 1948 over 1947, while imports remained approximately the same. As a result the trade deficit declined by about 14 billion francs. Since there is no reason to suppose that the balance on invisible account deteriorated, it may be estimated that the balance of payments deficit fell by at least 14 billion francs in 1948 from the previous year's level of approximately 15 billion francs. It appears that one of the important reasons for the large rise in exports during 1948 was the decrease in the relative attractiveness of the domestic market as a result of the decline in the growth of consumer demand, and possibly also

1/ Rapport sur les opérations de l'année 1948, Banque National de Belgique, 1949, p. 44

in the demand for capital goods, Likewise the failure of imports to increase during 1948 points to the same condition. It may be that, as in the case of Italy, the rapid progress toward balance of payments equilibrium was achieved partly at the expense of domestic investment.

Although the 14 billion franc reduction in the import surplus was expansionary, its effect on the Belgian economy was largely offset by a reduction in the budget deficit of about 10 billion francs. This improvement, which resulted from increases of 14 billion francs in receipts and 4 billion francs in expenditures, left a budget deficit of just over 10 billion francs in 1948. The provisional budget for 1949 envisages a further reduction to about 5 billion francs, but this expectation may not be realized because expenditures for unemployment insurance will rise and receipts may decline if incomes decrease significantly.

Whatever the initial cause of the recession it is probable that secondary effects have ensued. Possibly the initial impact was caused by a cessation of inventory accumulation at the end of 1947 which may well have been induced by a decline in the rate of growth of consumer expenditures. As orders were reduced, production was cut in marginal firms, marginal workers were discharged in an effort to cut costs, etc. As a result, consumer incomes were affected and this, in turn, began to influence consumer expenditures. Profit margins began to shrink in the wholesale and retail trades and employment was reduced there also. Whether fixed investment also declined is not known, but it is reasonable to assume that if a decline in capital formation was not a casual factor, such a decline would have been induced during the course of the year.

Summary and Conclusion

Unemployment began to appear in Belgium during the last quarter of 1947. Although the official production index had not yet declined as of November from the level of the fourth quarter of 1947, significant cuts in production have occurred in several consumer goods industries. On the other hand, production of metal products has continued to increase and a growing proportion of such production has been exported.

It would appear that the inventory boom which Belgium experienced during 1947 came to an end during the last quarter of that year and that this development was one of the factors which led to a decline in domestic demand for Belgian output. It is not yet possible to ascertain whether a decline in fixed investment was also a contributing factor to the softening in the economy. It is likely that consumer demand for non-food goods declined during 1948 not only because of "saturation" of the market by imported consumer goods earlier, but also because, after the abolition of subsidies, a growing proportion of family budgets was spent on food.

While declining foreign demand for Belgian textiles has probably been one of the factors responsible for the depression in that industry, its importance has apparently been exaggerated. In any case, total Belgian exports, and exports to Europe, have continued to increase in value and volume. In fact there is evidence that Belgian exporters, who had often charged considerably higher prices abroad than at home, have cut their foreign prices to some extent. Thus it appears that a growing proportion of Belgian output is being exported

while the volume of imports has decreased. Nevertheless, unemployment in Belgium has grown during 1948 and idle productive capacity has appeared.

What are the prospects for the future? The Belgian Government is preparing a public works program which will not only put unemployed labor to work, but is badly needed by the economy. Highways, bridges, and public transportation require improvement. For the longer run, however, it would appear that an acceleration of industrial investment is a necessity. The age of plant and equipment in Belgium is frequently cited by those who have fears for Belgium's ability to withstand competition when other European nations complete their reconstruction programs. Moreover one of the structural adaptations required by Belgium may very well be a reduction in textile output and an increase in the output of capital goods for export to developing countries.

The postwar prosperity in Belgium may to some extent be viewed as resulting from the difficulties of France, Germany and the Netherlands. As these countries recover and their production and exports increase, Belgium is likely to experience increasing competition both at home and in its export markets. The Belgian Government will face the problem of stimulating investment along the lines best suited to continued prosperity while adhering to its firmly-held policy of freedom from controls.

RELAXATION OF EXCHANGE CONTROLS IN BELGIUM AND FRANCE

R.S. and A.O.H.

Any country with a consistent system of exchange controls will ordinarily attempt to enforce a strict limitation on the import and export of its bank notes. This principle has been considerably relaxed by measures taken recently in France and Belgium.

Belgium: Paying for Exports in Belgian Franc Notes

In March 1949, the Belgian exchange control authorities issued a regulation making it permissible to import Belgian franc notes for the purpose of purchasing Belgian exports. Previously the foreign exchange proceeds of exports from Belgium were required to be paid to the National Bank of Belgium. Now Belgian exporters may be paid in francs purchased in one of the free markets outside of Belgium. All that is required is that the holder of such francs deposit them abroad into newly created "foreign-bank-note accounts" at a correspondent of an authorized Belgian bank. The accounts are freely transferrable among foreigners and may be used to purchase Belgian exports, as well as for expenditures within Belgium.

Before this action the Belgian franc note had been quoted at a discount of 15 to 20 per cent from the official rate in the various free markets of the world. As was expected the discount has declined and in New York it now amounts only to about 5 or 6 per cent. Temporarily at least a dual rate exists and the Federal Reserve Bank of New York is now certifying two rates for the Belgian franc for customs purposes. In this regard, it may be noted that the International Monetary Fund has not objected to the Belgian action. Apparently it was generally expected that the rate on franc notes would rise to the official rate in view of the fact that "foreign bank-note accounts" may be freely used for the purchase of Belgian exports thus providing American importers of Belgian goods with an incentive to purchase such franc notes instead of official exchange as long as a discount exists,

Two explanations for the persistence of the discount are possible. The first is simply that there is uncertainty and lack of knowledge concerning this new development, and, as soon as American importers realize fully what the situation is, the discount will be eliminated. Secondly, it is possible that this step has led to a large-scale conversion into dollars on the part of holders of Belgian franc notes in other countries and by European exporters to Belgium. The Belgian move opens up a convenient way for the citizens of other European countries to obtain dollars since facilities for obtaining Belgian francs are probably broader than those for acquiring dollars directly. This type of capital flow would have to reach large proportions relative to U. S. imports from Belgium which now amount to approximately \$10 million per month, in order to have the effect of maintaining the franc note at a discount from the official rate.

It should be noted that in countries which practice exchange control, foreign currencies may not legally be held by private citizens. Therefore, as far as legal transactions are concerned, there should be no effect on the exchange rate between the Belgian franc and other European countries. As long as the discount remains on the franc in terms of the dollar, the effect of the new step may be considered as an unofficial devaluation with respect to the dollar only.

What was the purpose of the Belgian move? As long as the discount continues and exports are stimulated there will be a favorable effect on employment in Belgium. The growing level of unemployment has begun to cause serious concern and, in fact, has become the foremost problem, economically and politically, in Belgium today. On the other hand, if the discount disappears the effect will have been to "harden" the Belgian franc and therefore perhaps to increase confidence in its stability. While this result may not contribute to the solution of Belgium's present unemployment problem, its longer-run effect may be an increase in foreign exchange reserves.

France: Capturing the Tourist's Foreign Exchange

In expectation of a good tourist season the French Government has recently devoted considerable attention to the study of measures by which the tourist could be made to convert his foreign exchange through legal channels rather than on the black market. The most important prerequisite for any success in this endeavor is a narrowing of the spread between official and black market rates. A large reduction in this spread has been accomplished as a result of the progressive financial and political stabilization of recent months. On the Paris black market the price for the dollar has fallen from 550 francs in December to 360 francs. The official "free" rate at which American tourists are supposed to convert their holdings is 318 francs so that the discount of the black market franc is only 11 per cent.

After having rejected the idea of compelling the tourist to convert, at the moment of entering France, a certain amount of foreign exchange per day of his planned stay, the French Government adopted a series of measures which attempt to achieve the desired result by means other than administrative compulsion. In the first place, hotels and casinos that are authorized to convert foreign exchange were permitted to retain 15 per cent of their dollar collections and 10 per cent of their collections in other foreign currencies for various legitimate expenses abroad or for sale in the official free market. This action which extends to hotels and casinos the privileges granted to

exporters is calculated to give to the hotels an incentive to bring some pressure on their customers to exchange their foreign exchange through legal channels. So far the personnel of the hotels had been very active in cooperating with the tourists in black market operations. Of greater importance is the successive raising of the amount in franc notes which foreign tourists are permitted to import into France, from 4000 francs before February to 40,000 at the end of March, or to about \$120 at current quotations.

This measure, therefore, legalizes to a significant extent the black market in foreign exchange. Although the foreign currencies exchanged against francs by the tourist in advance of his trip will not become available to the exchange control authorities, the measure may have a subtle rationale: the demand for francs against dollars in the black market will be exerted at an earlier date than would otherwise be the case. In this way, the spread between the official and black market rates will be further reduced by the time the main body of tourists arrives in France, so that at that time the incentive to go to the black market for their further franc needs is expected to be quite small. In effect, the new regulations introduce a new official franc rate for tourists into which the black market rate enters as a component. The average of this tourist rate is the more favorable to the tourist the less his total expenditures exceed 40,000 francs. The International Monetary Fund has not objected to the French action.