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Board of Governors of the Federal Reserve System
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# REVIEW OF FOREIGN DEVELOPMENTS

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## UNITED STATES FOREIGN TRADE IN JANUARY-MARCH 1949

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The outstanding developments in U.S. foreign trade in the first quarter were a continued expansion in exports and the leveling off of imports. The upward trend in exports which commenced in the final quarter of 1948, after a persistent decline during the previous five quarters, was continued in the January-March period. The rise in exports to the early 1948 rate, which has been anticipated for some time, reflects in the main the effect on our exports of dollars available under the E.C.A. program.1/ In fact, with reduced foreign aid funds available, the impact of the E.C.A. program on our exports is probably at a maximum. On the import side, 1949 imports, although maintained near the 1948 level, fell slightly below the value for the same period last year. This is the first time since the end of the war that quarterly imports have fallen below the corresponding figure for the preceding year. The rapid post-war expansion in imports may thus be coming to a halt, perhaps because of declining business activity in this country.

Table I
United States: Exports and Imports by Quarters
(In millions of dollars)

| | I | II | III | IV |
|---|---|---|---|---|
| Exports: | | | | |
| 1946 | 2,284 | 2,485 | 2,352 | 2,620 |
| 1947 | 3,774 | 4,181 | 3,716 | 3,674 |
| 1948 | 3,317 | 3,237 | 2,935 | 3,126 |
| 1949 | 3,277 | | | |
| Imports: | | | | |
| 1946 | 1,096 | 1,181 | 1,230 | 1,402 |
| 1947 | 1,412 | 1,449 | 1,323 | 1,549 |
| 1948 | 1,810 | 1,710 | 1,729 | 1,875 |
| 1949 | 1,790 | | | |

U.S. exports in the first quarter of 1949, valued at $3,277 million, were about $40 million below actual exports in the first quarter of the previous year. This slight decline in value, however, obscures the significant expansion in the physical volume in 1949 compared with the earlier year. For the unit value of exports, which has been dropping persistently since July 1948, averaged in January-March this year about 5 per cent below the average for the first quarter of 1948. The quantity index rose about 4 per cent between the two periods. Preliminary data for April show a continuation of the recovery of exports from the low level reported in the third quarter of last year. In fact, exports for the four months, January to April, totaled $4,424 million, only $13 million below the value for the same four months in 1948.

1/ See this Review, November 30, 1948, p. 6.

The continued expansion in imports, which has characterized the post-war period, was arrested in the first quarter, but their value is being maintained near the high 1948 levels. Due to some increase in import prices the volume of imports was about 4 per cent below the movement for the first three months of 1948. Imports for the four months, January to April, amounted to $2,324 million, only about $18 million below the total for the same period in 1948. The relative stability in import prices, shown in Table II, contrasts with other American price trends. The leveling off of import volume may, in part, reflect the first effects of the decline in American business activity and, in part, the expectation of importers that price adjustments are to be anticipated in the near future. The trend in imports has been the opposite of the trend in exports: import prices were maintained and volume reduced while export prices have declined and quantity has increased with respect to the first quarter of 1948.

Table II
United States: Indexes of Unit Value of Exports and Imports
Monthly, January 1948 to March 1949
(1923-25 = 100)

| Month | Export | Import | Month | Export | Import |
|---|---|---|---|---|---|
| 1948: | | | | | |
| January | 137 | 126 | July | 138 | 133 |
| February | 139 | 130 | August | 135 | 133 |
| March | 136 | 131 | September | 133 | 135 |
| Average | 137 | 129 | Average | 135 | 134 |
| April | 136 | 132 | October | 133 | 133 |
| May | 136 | 131 | November | 132 | 133 |
| June | 136 | 130 | December | 131 | 133 |
| Average | 136 | 131 | Average | 132 | 133 |
| 1949: | | | | | |
| January | 132 | 133 | | | |
| February | 130 | 133 | | | |
| March | 128 | 130 | | | |
| Average | 130 | 132 | | | |

The check to the expansion of imports appears to indicate that the pre-war relation between imports and gross national product has been fundamentally altered by wartime developments. Important structural changes in the American economy can easily explain this change but, because American imports continued to expand vigorously, many observers looked upon the difference between actual imports and projected imports as a temporary gap, and noted that there has been a tendency since 1945 for the gap to be narrowed. It would appear, however, that the hope that imports will return to their pre-1939 relationship can no longer be sustained.

The export surplus for the first quarter amounted to $1,487 million compared with the 1948 total of $1,506 million. The first quarter's surplus was, therefore, at an annual rate of $5,948 million compared with the actual 1948 surplus of $5,491 million. The increase in the quarter rate over the actual 1948 figure, however, is mainly due to seasonal factors. Data for the four months including April show a slight rise in the annual rate of the surplus of $6,301 million compared to $6,286 million for January-April 1948.

Table III
United States: Export Surplus by Major Areas, by Quarters
(In millions of dollars)

| | Annual Average (quarterly rate) | | | First Quarter | | |
|---|---|---|---|---|---|---|
| | 1946 | 1947 | 1948 | 1947 | 1948 | 1949 |
| Europe | 825 | 1,216 | 797 | 1,297 | 937 | 881 |
| 13 E.R.P. countries | 597 | 941 | 496 | 991 | 613 | 589 |
| 4 Special-aid countries a/ | 53 | 208 | 311 | 203 | 293 | 281 |
| Total 17 E.R.P. countries b/ | 650 | 1,149 | 807 | 1,194 | 906 | 870 |
| North America | 224 | 421 | 214 | 410 | 185 | 173 |
| South America | 14 | 279 | 92 | 262 | 124 | 88 |
| Asia | 113 | 322 | 190 | 264 | 194 | 256 |
| Australasia | -17 | 41 | -3 | 16 | -6 | 20 |
| Africa | 46 | 124 | 95 | 113 | 81 | 61 |
| Total | 1,205 | 2,403 | 1,385 | 2,362 | 1,515 | 1,479 |

a/ Germany, Austria, Greece, and Turkey.
b/ Includes Turkey.

The data on the export surplus for the first quarter, shown in Table III, show no marked change from the first quarter of 1948 although the reduction from the high 1947 figure is substantial. Between 1948 and 1949, the surplus for the 17 E.R.P. countries declined about $35 million with both the 4 special-aid and 13 other E.R.P. countries participating in the reduction. The export surplus with Latin America shows a steady drop from the first quarter of 1947, reflecting dollar stringency. On the other hand, the 1949 surplus for Asia and Australasia was significantly higher than in 1948, returning in both instances to the rate reported for the first three months of 1947.

Trade by commodities

Although total exports for 1949 were about the same as the previous year, there were some shifts in the commodity composition. Finished manufactures, though continuing to comprise over half of U.S. exports, were down by about $170 million. Manufactured foodstuffs showed a $90 million reduction. The major commodity groups participating in these declines were merchant vessels, cotton manufactures, automotive equipment, wheat flour and fruit products. By contrast, exports of crude materials and crude foodstuffs rose substantially. Heavier shipments of grain and cotton were responsible for these increases.

Table IV
Distribution of U.S. Merchandise Trade, by Economic Classes
January to March, 1947 to 1949
(In millions of dollars)

| | Exports | | | Imports | | |
|---|---|---|---|---|---|---|
| | 1947 | 1948 | 1949 | 1947 | 1948 | 1949 |
| Crude materials | 431 | 329 | 466 | 460 | 573 | 502 |
| Crude foodstuffs | 319 | 322 | 397 | 288 | 346 | 340 |
| Manufactured foodstuffs | 455 | 341 | 251 | 134 | 162 | 181 |
| Semi-manufactures | 384 | 389 | 385 | 281 | 396 | 397 |
| Finished manufactures | 2,125 | 1,904 | 1,733 | 231 | 295 | 336 |
| Total | 3,713 | 3,285 | 3,232 | 1,396 | 1,772 | 1,756 |

The shifts in the composition of imports were opposite to the changes in exports. The largest increase was shown in finished manufactures. Newsprint and machinery and vehicles were the major commodity groups reporting rises. Imports of crude materials, on the other hand, were sharply reduced, although they were still higher than in the first quarter of 1947. The reductions in shipments in the crude materials group were distributed among a number of commodities, and were marked for wool, hides and skins, furs, oilseeds and rubber.

Trade by area

The distribution of exports by area in 1949 showed little change from the previous year. Increases were reported for North America and Asia, with Canada, Japan, Netherland Indies, Iran and Taiwan accounting for the rises. The major reductions were in the movement to South America, Europe and Africa, especially Argentina and South Africa. Shipments to the 17 E.R.P. countries were only slightly reduced.

Table V
Distribution of U.S. Merchandise Trade, by Area
(In millions of dollars)

| Area | Exports | | | Imports | | |
|---|---|---|---|---|---|---|
| | 1947 | 1948 | 1949 | 1947 | 1948 | 1949 |
| North America | 906 | 790 | 831 | 496 | 606 | 657 |
| South America | 571 | 549 | 471 | 310 | 425 | 383 |
| Europe, total | 1,483 | 1,206 | 1,151 | 186 | 269 | 270 |
| 17 E.R.P. countries | 1,367 | 1,141 | 1,119 | 173 | 235 | 250 |
| 4 special-aid " | 234 | 323 | 319 | 31 | 31 | 39 |
| 13 other E.R.P. " | 1,133 | 818 | 800 | 142 | 204 | 211 |
| Other Europe | 133 | 84 | 41 | 36 | 46 | 34 |
| Asia | 568 | 532 | 598 | 303 | 338 | 342 |
| Australasia | 64 | 42 | 54 | 47 | 48 | 34 |
| Africa | 183 | 198 | 163 | 70 | 116 | 103 |
| Total | 3,775 | 3,317 | 3,268 | 1,412 | 1,802 | 1,789 |

Only minor shifts occurred in the origin of American imports. The major area showing an increase was North America, due almost entirely to a continued high level of imports from Canada. The sharpest curtailment came from South America with the reduction from Argentina accounting for most of the cut.

The increasing percentage of imports from the 17 E.R.P. countries reflects some recovery progress. Thus, these countries provided $250 million of U.S. imports in the first quarter, compared with $235 million in 1948 and $173 million in 1947, as shown in Table VI. With U.S. imports slightly reduced, the E.R.P. countries accounted for 14.0 per cent in 1949 compared with 13.1 per cent for the previous year. Yet compared with the 24.5 per cent of imports supplied in 1938, the progress is relatively limited. Analysis of country data, in fact, reveals that some countries are already encountering real difficulties in the American market. The decline in imports from Sweden and the United Kingdom are examples of this development. Belgium made striking progress in the first quarter of 1949, however, and Germany, Norway, and the Netherlands also recorded some improvement.

Table VI
United States: Imports from 17 E.R.P. Countries, Quarterly
(In millions of dollars)

| | Quarterly Average | | | | First Quarter | | |
|---|---|---|---|---|---|---|---|
| | 1938 | 1946 | 1947 | 1948 | 1947 | 1948 | 1949 |
| Imports from 17 E.R.P. countries | 120 | 170 | 174 | 240 | 173 | 235 | 250 |
| Total U.S. imports | 490 | 1,227 | 1,433 | 1,769 | 1,412 | 1,802 | 1,789 |
| Per cent | 24.5 | 13.8 | 12.2 | 13.6 | 12.3 | 13.1 | 14.0 |
| By country: | | | | | | | |
| United Kingdom | 30 | 39 | 51 | 72 | 47 | 73 | 68 |
| Belgium and Luxembourg | 10 | 19 | 15 | 22 | 14 | 18 | 37 |
| France | 14 | 16 | 12 | 18 | 14 | 16 | 18 |
| Italy | 10 | 17 | 11 | 24 | 12 | 20 | 20 |
| Netherlands | 8 | 6 | 7 | 11 | 4 | 7 | 12 |
| Sweden | 11 | 12 | 23 | 23 | 15 | 31 | 12 |
| Switzerland | 6 | 25 | 21 | 26 | 22 | 23 | 24 |
| Turkey | 5 | 17 | 14 | 13 | 23 | 12 | 14 |
| 8 Other countries | 27 | 19 | 21 | 31 | 23 | 36 | 44 |

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THE BERLIN CURRENCY CONTROVERSY Gordon Grimwood

The Berlin currency controversy arose in June 1948 as an offshoot of a larger political controversy between the Western powers (the United States, the United Kingdom, and France) and the Soviet Union over the problem of a general German currency reform. It was recognized that such a reform was badly needed. The German economy was burdened with an excess of money in circulation; hoarding was widespread and transactions often took the barter form. Although broad general agreement on the issues involved had been reached, a quadripartite discussion continued for many months on technicalities until the Western powers, accusing the Soviets of delaying tactics, announced on June 18, 1948, a currency reform to be effective in the three Western Zones on June 20, 1948. 1/

Recognizing the special economic status of the City of Berlin, the Western powers exempted their sectors of that city from the currency reform. The Soviet Military Authority, however, immediately protested the unilateral action of the Western authorities in proclaiming a currency reform for their zones and, after the failure of a quadripartite discussion in Berlin on June 22, 1948, the Soviet commander closed the border of the Soviet Zone, allegedly to prevent the entry of a flood of Reichsmarks rendered worthless by the Western currency reform. On June 23, 1948, he announced a currency reform for the Soviet Zone of Germany and all of Greater Berlin. 2/ It thus became necessary for the Western authorities to extend their currency regulations to their sectors of Berlin.

On June 23, 1948, therefore, the military commanders of the Western Zones announced a currency reform for Berlin which was in most respects similar to the regulations promulgated in the three Western Zones on June 18, 1948. 3/ In order to limit the circulation of the Westmark, as it came to be called, it was directed that wages were to be paid 75 per cent in Eastmarks and 25 per cent in Westmarks, the Eastmarks being acceptable for payment of rent, food, taxes, and utility bills. Shopkeepers and other business enterprises could accept either currency at their option. In order to conserve the Westmarks for the Berlin economy, the Western authorities on July 24 limited the number of Westmarks which could legally be taken from the city to DM 300. German marks which had been brought in to circulate in Berlin had been overprinted with a large "B" in a circle to distinguish them from the currency circulating in the three Western Zones.

On July 24, 1948, the Soviet Military Authority announced a second currency conversion for the Soviet Zone, replacing the stamped Reichsmarks issued on June 23 with permanent German marks issued by the Deutsche Notenbank in that Zone. This conversion took place between July 25 and July 28, the ratio of exchange being one new mark for one old one up to 70 marks, any balance to be

1/ OMGUS Report No. 36, June 1948.
2/ OMGUS Report No. 37, July 1948.
3/ This Review, July 13, 1948, p. 3.

paid on August 15 also at a 1 for 1 rate. During this conversion Western Berliners lost a large, though indeterminate, amount of the value of their holdings of Eastmarks because of the shortness of the conversion period. It was also reported that the Soviet authorities arbitrarily declared a large percentage of such marks to be counterfeit.

The double currency situation, added to the tenseness of the political atmosphere, resulted in complete confusion for the Western Berliners. Unemployment rose sharply during July, due to the effect of the Soviet blockade rather than the currency reform, and the workers' distress was further increased by a Soviet order of July 30, 1948, which blocked all accounts of Western Berlin firms held in Soviet sector banks, including that of the Berlin Magistrat (the German civil ruling body of Berlin). The Western authorities found it necessary to open official money exchange booths in order to obtain sufficient Eastmarks to meet current government obligations; the rate of exchange, which under normal circumstances would be indicative of the relative values of the currency, varied more for political than for economic reasons, dropping from 1 Westmark for 20 Eastmarks to 1 for $1\frac{1}{2}$ as the citizens of Berlin began to fear that the Western powers would be forced out of Berlin. This rate later stabilized at about 1 Westmark for 3:50 to 4 Eastmarks. It was estimated that during July West Berlin industrial production dropped to around 20 - 25 per cent of capacity, 1/ a level which was to be maintained during the period of the blockade.

Because of the blocked accounts neither the city government nor private firms were able to meet their payrolls, and the monetary shortage became acute. Negotiations carried on by the Western and Soviet authorities through the Magistrat on the one hand and authorities of the Soviet-controlled Deutsche Notenbank on the other, resulted in August 5 in a Soviet agreement to release the blocked accounts. On August 6, however, it was discovered that the Deutsche Notenbank would release the blocked funds of private firms only for purposes of trade with Soviet-controlled trading companies in the Soviet zone, a condition which a majority of Western sector firms refused to accept. The City Magistrat, however, received 25 million Eastmarks.

On August 1 there began in Moscow a conference of the foreign ministers of the United States, United Kingdom, France, and the Soviet Union which pointed up the issues of the Berlin situation very clearly. The Soviets were willing to lift the blockade only if the Western powers withdrew their currency; the Western powers were willing to withdraw their currency only if they were assured some control over the Soviet currency to circulate in Berlin.

The Western powers had good reason to desire such control before reaching an agreement. It was estimated that, while the currency reform in Western Berlin had mopped up 9/10 of the excess purchasing power, the reform in the Soviet Zone of Germany had taken care of only 1/4 to 1/3 of the excess purchasing power because they had exchanged new marks for old at a 1 for 1 ratio for

1/ OMGUS Report No. 37, July 1948.

all Soviet personnel, Communist Party organs, and Soviet-controlled trading companies. 1/ Uncontrolled circulation of Soviet currency in Berlin would mean that goods produced in Western Berlin or imported from the Western Zones would be purchased with inflated Soviet currency and disappear into the Soviet Zone or beyond without any reciprocal return of goods. On August 30, 1948, the foreign ministers' conference reached a broad agreement based on these considerations and directed the military commanders of the occupied zones of Berlin to confer in order to implement that agreement.

The quadripartite discussion at military government level began on August 31, 1948, and lasted through September 7. Negotiations broke down because the Soviet military commander refused to interpret the broad language of the directive from the foreign ministers' conference to include control of the circulation of currency in Berlin. The Western military governors refused to agree to a single currency in Berlin without such control, the Soviets refused to lift the blockade until such a currency existed, and the situation remained unchanged.

On September 6, 1948, a meeting of the Magistrat in its building in the Soviet sector of Berlin was broken up by German Communists with considerable violence, and the City of Berlin has had, in effect, two city governments since that date.

Following the breakdown of negotiations between the Western and the Soviet military governors, the Western powers decided on September 26, 1948, to present the case to the United Nations Security Council. The Security Council appointed a Technical Committee on Currency and Trade in Berlin, which drew up a list of questions to be studied by representative experts from the countries involved in the dispute in an effort to find some common ground upon which an agreement might be based. Replies received from the Western and Soviet experts revealed that the major point of issue was that of control of the circulation of currency in Berlin. The Soviet authorities feared that such control might be used to interfere with currency and credit in the Soviet Zone, since the same currency would be used in Berlin, while the Western authorities continued to oppose an uncontrolled circulation of Soviet Zone currency in their sectors of Berlin. The Western experts also pointed to the difficulties inherent in establishing control over currency circulation in a city rapidly being divided into two cities. Originally the Western powers had proposed that the "Stadtkontor should act as the central bank of Berlin and, together with the Deutsche Notenbank, the bank of issue for the Soviet Zone, serve as the organ through which a quadripartite Financial Commission would control the circulation of currency in Berlin. Since the Stadtkontor was located in the Soviet sector, however, the Western powers declared that the establishment of Soviet-dominated city authorities in that sector nullified their proposal. In effect, both parties to the dispute accused the other of violating the four-power directive of August 30, 1948, basing the accusations on differing interpretations of that directive.

1/ "Banking in the Soviet Zone", S. Schattmann, The Banker, October 1948.

The Security Council's Technical Committee, after considering the documents submitted by the experts of the Western powers and the Soviet Union, prepared a draft recommendation which was based on those replies and upon the Committee's terms of reference, i.e., the four-power directive of August 30, 1948. This recommendation proposed to solve the Western objections to the circulation of a single currency in Berlin by limiting that circulation to a specified fraction of the initial issue of Soviet-Zone currency; such circulation should be changed only with the approval of a four-power Financial Commission. The Soviet fears of interference in their zone of occupation were to be allayed by providing for controlled price and wage structures and banking regulations, to be set for all of Berlin by the Financial Commission. Interzonal trade was to be conducted on a net-balance basis under the strict control of the Financial Commission. All decisions of the Financial Commission were to be unanimous. The Committee then presented detailed recommendations intended to implement their broad general recommendations.

The remarks of the Soviet expert, presented to the Committee on January 3, 1949, suggested revisions which would result in the establishment of four-power control of Berlin under conditions closely akin to those existing in the Soviet Zone at that time, especially by tying the proposed wage, price, and tax rates to existing Soviet Zone rates. The Soviet expert also wished to bring the city's economy under more detailed control of the Financial Commission, as indicated by his suggestion that the city budget be subject to the approval of the Commission.

The expert of the United States, Mr. J. Burke Knapp, in a memorandum to the Technical Committee dated January 15, 1949, criticized the draft recommendation as based on the assumption of a unified city, whereas in fact the city was and would probably remain divided. He pointed out the advantage which the veto power gave to the Soviet authorities in the Finance Commission, and stated that under such circumstances the Western powers could consider such quadripartite control only if concrete regulations were spelled out in the agreement setting up the Commission. He also noted the "jockeying for position" which would occur under the voting procedure considered by the Technical Committee for the German agencies to be established to implement the decisions of the Finance Commission. He criticized the policy of fixing the amount of currency in circulation on the basis of the original issue, stating that there was considerable reason to believe that such a ratio would not be equitable. In this connection he referred to the impossibility of determining what amount of Soviet Zone currency would have been issued in Western Berlin, the unreliability of Soviet Zone statistics, and the necessity for strict currency controls under such a system. The U. S. expert submitted as annexes to this memorandum a detailed technical criticism of the Committee's draft recommendation and his own proposed solution to the controversy.

This proposal was based on the acceptance of a divided Berlin. A Western Sector central bank would established, to which the Soviet Zone bank of issue would furnish Eastmarks in an amount sufficient to carry out a conversion of Westmarks held by Western Berlin inhabitants to Eastmarks under the supervision of a Neutral Committee to be established by the agreement. After the conversion, Eastmarks would be furnished to the Western Sectors in an amount sufficient to carry on ordinary business operations. This supply of Eastmarks would be curtailed if, in the judgment of the Neutral Committee, inflationary pressures appeared in the Western sectors and pushed prices in those sectors above prices in the Soviet sector by a specified margin. The Western powers would reserve the right of regulating all "foreign" trade of Western Berlin, including interzonal trade. The Western powers would also retain the unrestricted right of regulating and supervising budgetary operations of the Western Magistrat.

Also on January 15, 1949, the French and English experts submitted identical memoranda which conformed very closely to the criticisms and suggestions presented by the U. S. expert.

On January 20, 1949, the Technical Committee forwarded to the Soviet expert the suggestion of the U. S. expert, requesting his comments thereon. In a short reply dated January 25, 1949, the Soviet expert rejected the suggestion as a basis for discussion on the grounds that it did not conform to the four-power directive of August 30, 1948. A memorandum from the combined experts of the United States, United Kingdom and France dated February 4, 1949, pointed out the wide area of disagreement existing between the Western powers and the Soviet Union on the basis of the draft recommendation, and urged further consideration of the suggestion of the U. S. expert. The Soviet expert, in a reply dated February 11, 1949, accused the Western powers of breaking an agreement to use the draft recommendation as a basis for discussion and of ignoring the four-power directive of August 30, 1948. The Soviet expert expressed the willingness of the USSR to negotiate on the basis of the draft recommendation, stating that the refusal of the Western powers to accept the draft "proved the reluctance of the Governors of the three Western Powers to arrive at an agreement on the problem at issue".

On February 11, 1949, the Technical Committee on Currency and Trade in Berlin submitted its report to the President of the Security Council stating that, due to the wide area of disagreement, the Committee could see no further use for its services. The Committee made no recommendation since, due to the lack of agreement between the parties to the dispute, it was precluded from doing so by its terms of reference. The Committee also refrained from any analysis of the dispute, contenting itself with a presentation of both sides of the argument.

The opposed positions of the Western Powers and the Soviet Union were indicated during the early part of February 1949 when an exchange of notes between Premier Stalin and Secretary of State Acheson revealed that the Soviets would refuse to lift the Berlin blockade until the West withdrew its currency from the Western sectors of Berlin and agreed to discuss the entire problem of Germany at the foreign minister level, while the Western powers would refuse to negotiate on any of these issues until the blockade was lifted.

During February and the early part of March tripartite discussions of the feasibility of banning the Eastmark from the Western sectors of Berlin continued. It was pointed out that the dual currency situation resulted in unfair discrimination against the workers who were employed by firms having no markets in the West. These workers could draw their wages only in Eastmarks, which had about one-fourth the value of Westmarks. It was also pointed out 1/ that Berlin manufacturers, hampered by the lack of power and raw materials and the cost of transport, were enabled to compete in the Western Zones only by being subsidized through the privilege of exchanging Eastmarks for Westmarks on a 1 for 1 basis. This subsidy was being borne by the Berlin treasury.

On March 20, 1949, the Third Ordinance for Currency Reform, promulgated by the military commandants of the Western sectors of Berlin, provided for the Westmark to become the exclusive legal tender in the Western sectors of Berlin. Possession or use of the Eastmark was not prohibited, but the Eastmark was no longer legal tender for payment of rent, taxes, food rations, utility bills, etc. In order to absorb the floating supply of Eastmarks, holders of such currency were permitted to buy rationed food and special food allocations with that currency until March 31, 1949. All holders of ration cards in the Western sectors were permitted to exchange 15 Eastmarks for 15 Westmarks at a 1 for 1 ratio, and to pay half of their April rent and a certain percentage of taxes in Eastmarks. Business firms were permitted to exchange the equivalent of two weeks' wages in Eastmarks for Westmarks at the 1 for 1 ratio, and those concerns subject to turn-over taxation were permitted to exchange the equivalent of 5 per cent of one months' turnover at the same rate. Provision was also made in the Ordinance for those inhabitants of the Western Sectors who worked in the Soviet sector and drew pay, rations, or both in that sector. On the same date the Fourth Ordinance for Currency Reform established the Berlin Central Bank, which was given the power to regulate the circulation of currency and the supply of credit.

The economic situation in the Soviet sector of Berlin during the period under review (indeed, in the entire Soviet Zone in Germany) was fully as bad as, if not worse than, the situation in the Western sectors of Berlin, and much worse than the situation in the Western Zones of Germany. A report submitted by the Bizonal Economic Administration for February 1949 showed that the food rations for the two zones were very nearly identical, with the Soviet Zone having a slight edge as to quality (fresh as compared with canned foods, etc.) Since the Soviet currency reform of July 24, 1948, had not gone far enough in mopping up excess purchasing power and the effects of the Western counterblockade had resulted in very short supplies of consumer goods, prices of available supplies were highly inflated. On February 18, 1949, a rumor of impending currency reform in the Soviet Zone caused a panic during which the exchange rate of the Eastmark fell as low as 18 to 1, bringing bitter Soviet charges that the panic had been engineered by Western Berlin speculators as a device to cheat the small wage-earner of his money.

In view of these conditions, and of the continuing success of the air lift, conversations took place between Dr. Jessup and Mr. Malik, U. S. and Soviet delegates to the United Nations, respectively, which resulted in the lifting of

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1/ "Report of Bizonal Economic Administration, February 1949", Consular Report 488, Berlin, April 21, 1949.

the Berlin blockade on May 12, 1949, and the convening of a foreign ministers' conference on May 23. The agreement resulting in the lifting of the blockade made no mention of the Berlin currency question; it is a part of the larger problem of unifying Berlin, a problem which is at present under discussion in Paris.

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RECENT BRITISH INVESTMENT EXPERIENCE IN IRAN Mary Maroney

The current exploration of overseas investment opportunities for U. S. capital, and the effort to develop guarantees which will be reassuring to investors, lend some interest to recent British investment experience in Iran. In banking and oil production, the two fields in which British investment has been important, the Iranian Government has made serious moves to revise existing concessions. It appears that the country's ambitions for development with the aid of foreign capital are now accompanied by a distinctly harder attitude as to the terms of participation. The Iranian authorities, as those of other underdeveloped countries, aim at obtaining a greater share of the revenue and a higher degree of control over the foreign investments.

The Imperial Bank

The main British investment in banking is the Imperial Bank of Iran, the principal commercial bank of the country, which has branches in all the important cities of Iran as well as in most other Near Eastern countries. The charter of this 60-year-old institution has recently come up for renewal, and the Government has taken this occasion to promulgate a decree greatly affecting the Bank's future sphere of operations.

The decree provides that foreign banks operating in Iran must turn over to the Bank Melli (the Iranian central bank) acceptable foreign exchange in an amount equivalent to their capital and reserves, and must hold with the Bank Melli without interest at least 55 per cent of their time and demand deposits. The maximum amount of deposits which they are allowed to retain may not exceed 225 per cent of capital and reserves up to 260 million rials (£2 million at the official exchange rate of 130 rials to the £) plus 100 per cent of any increase in capital.

The Imperial Bank has had capital and reserves totalling £2 million and deposits of about £10 million in local currency. Of the latter, £5.5 million will, under the new regulation, have to be turned over to the Bank Melli and therefore will cease to be convertible into earning assets. Moreover, the bank will be required to transfer to Iran from London £1 million sterling which must be sold to the Bank Melli for local currency. The bank will be permitted to use its properties in Iran, valued at an additional £1 million, for making up the remainder of the equivalent of £2 million in capital and reserves which under the new decree would have to be sold to the Bank Melli in foreign exchange.

This development had been foreshadowed by a decree of November 1946, requiring commercial banks to hold 15 per cent of their demand and 6 per cent of their time deposits with the Bank Melli without interest. The Imperial Bank had voluntarily invested, in addition, a like proportion of deposits in Iranian Government bonds. Together, these items accounted for almost 30 per cent of total deposits, time deposits being quite small in relation to demand deposits. The new regulation, therefore, represents a critical increase in reserve requirements. It not only puts the central bank in control of a major portion of the

Imperial's assets but may even result in some contraction of the latter's loan portfolio. Currently this portfolio approximates £5 million; however, the deposits remaining after deduction of the 55 per cent requirement will be only £4.5 million. The local currency resulting from the forced sale of £1 million to the central bank will hardly cover the difference between that sum and the present loan portfolio plus till money requirements in local currency reported to be in the neighborhood of £0.8 million.

Although stiff enough, these requirements represent the result of bargaining which began from a much more stringent base. The decree was obviously drafted to fit the exact conditions of the Imperial Bank. There is only one other foreign bank (Soviet-Iran) which will be affected; however, this bank does not conduct commercial business except for transactions carried out for the Soviet Government.

The Anglo-Iranian Oil Company

The oil situation affects primarily the Anglo-Iranian Oil Company, which is at present the sole producer in Iran (and the largest producer in the entire Middle East) and Iran's largest enterprise. It is a British company, and 56 per cent of its share capital is owned by the British Government. Under the existing concession the Iranian Government receives, in addition to royaltie which are paid on tonnage production, 20 per cent of the profits in excess of £671,250 whether declared as dividends or added to reserves. The Iranian Government feels that this share of the profits is too small because it is calculated after rather than before taxation imposed on the company by Great Britain. It makes the point that it is in effect paying taxes to the British Government and it is asking for revision of the terms of the concession. The company's annual report for 1947 (the latest available) showed record trading profits of £33.4 million inclusive of profits realized from its oil interests in Iraq and Kuwait. United Kingdom taxation, however, took £14.8 million so that the amount available for reserves and dividends was reduced to £18.6 millio Iran's total receipts from the concession in 1948 were estimated at approximately £9 million.

Greater Iranian participation in the management of the Company is also being sought. A considerable number of local personnel is already employed, in pursuance of the terms of the concession, but not on the policy level. The revision of the concession is still being discussed.

These two developments have more than casual significance in relation to the country's ambitious Seven-Year Development Plan, which was voted by Parliament in February. This program envisages the investment of about $650 million which are to be allocated as follows: agriculture, $164 million; railroads, roads, ports, and airports, $156 million; industry and mines, $94 million; petroleum, $31 million; posts and telegraphs, $23 million; social and municipal reforms, $188 million. The Iranian Government has employed American engineering companies to make detailed surveys of various projects connected with the Seven-Year Plan.

The magnitude of the project is roughly indicated by comparison with the ordinary budget for the period March 1948 to March 1949, which is based on revenue estimated at 6.1 billion rials excluding oil royalties (188 million at the official rate of exchange of 32.50 rials per dollar). 1/

Financing of the program is planned from three principal sources; viz., (1) the government's oil royalty receipts, which, in view of the circumstances above outlined, and as a result of the expansion of oil production, seem likely to increase. Under present conditions it is estimated that about $250 million will be available in seven years from this source; (2) borrowing from the International Bank for Reconstruction and Development to the extent of $250 million; (3) borrowing from the Bank Melli Iran to the extent of $140 million. There is apparently a connection between this last proposal and a bill recently introduced by the Government to change the currency reserve requirement which calls for a reduction in the note cover from the present 60 per cent in gold and foreign exchange to 50 per cent, one-half of which is to be held in gold. Currently the Bank Melli's gold and foreign exchange holdings cover 78 per cent of the circulation. Going over to a 50-per cent cover would permit additional circulation of 4.4 billion rials ($138 million).

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1/ Conversions of rials into United States dollars and pounds sterling have been made at the official rates because these rates apply to all Government transactions. The "free" rates used in commercial transactions give the rial a considerably lower value (50.75 to the dollar and 200 to the pound sterling, as of March 1949, the latest date available).