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REVIEW OF FOREIGN DEVELOPMENTS

June 20, 1950

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June 22, 1950UNITED STATES FOREIGN TRADE IN JANUARY-APRIL 1950Arthur B. Hersey and
Gretchen H. Fowler

Statistics for United States exports and imports in April provide additional confirmation of the very significant adjustment which has now been made in this country's export surplus. In 1948, recorded exports exceeded imports by \$5.5 billion. By the first four months of 1950, the export surplus had been cut to \$2.2 billion (annual rate).

The following notes are intended to review briefly the process by which the adjustment of the export surplus has been made, and to give some indications of the nature of present United States import demands and of the cuts that have been made in foreign countries' demands for our exports. The basis of comparison is taken as 1948, since 1949 was a year of sharp and divergent changes: exports dropped at the middle of 1949, and imports fell and rose along with the recession and recovery of business in the United States.

It is significant that the annual rate of the export surplus in April, \$2.7 billion, was only moderately higher than the \$2.0 billion average in the first quarter; seasonal variations in imports played a part in raising the April surplus. It is already virtually certain that the total export surplus for the calendar year 1950 will be much smaller than in 1948. Although trends in exports are difficult to predict it appears unlikely that a sharp rise of U.S. exports will take place this year. Recent increases in market prices for imported raw materials furnish grounds for expecting a further rise in recorded import values.

The Adjustment of the Export Surplus

Timing.-- The reduction in the export surplus began and was largely accomplished during the second half of 1949. ^{1/} In the first half of 1949, the gap had been even larger than in 1948. Exports, after remaining at relatively high levels throughout 1948 and the first half of 1949, dropped sharply in the third quarter and then continued to fall off until February 1950. Imports, which had been at a post-war high in 1948, declined in the first half of 1949, temporarily increasing the export gap. After July, however, monthly imports rose steadily, contributing to a reduction of the gap. Imports in the first quarter of 1950 at an annual rate of \$7.6 billion, were actually above the earlier peak rate of the fourth quarter of 1948. Exports, however, had fallen ~~one~~ fourth below 1948, levelling off in the first quarter at a rate of \$9.5 billion.

^{1/} See this Review, January 3 and April 25, 1950.

Table 1

Export Surplus, 1/ 1948-50
(Billion dollars, annual rate)

<u>Period</u>	<u>Export Surplus</u>	<u>Exports</u>	<u>Imports</u>
Year 1948	5.5	12.7	7.1
<u>Quarters</u>			
1948 - I	6.0	13.3	7.2
- II	6.1	13.0	6.8
- III	4.8	11.7	6.9
- IV	5.2	12.7	7.5
1949 - I	6.1	13.3	7.2
- II	7.0	13.4	6.4
- III	4.8	10.7	5.9
- IV	3.5	10.5	7.0
1950 - I	2.0	9.5	7.6
1950 - April	2.7	9.7	7.0

1/ Recorded merchandise trade; exports of U.S. merchandise and reexports; general imports.

Quantity and Price Factors.-- Of the \$3.5 billion reduction in the export gap between 1948 and the first quarter of 1950, \$1.9 billion may be ascribed to a decrease in the quantity of exports (valued at 1948 prices), \$0.8 billion to an increase in the quantity of imports, and \$0.8 billion to the changed prices at which exports and imports were moving in the early part of 1950. There was a price saving of \$1.2 billion to buyers of our exports and a \$0.4 billion addition through the price factor to our expenditures for coffee in the first quarter, but these were partly offset by a price saving to us of \$0.8 billion on our imports other than coffee 1/.

Imports

The decline and subsequent recovery of imports in 1949 was doubtless caused mainly by the simultaneous swing in U.S. business activity. Some of the shift may have been caused by a postponement of purchases in the summer when there were rumors of impending devaluations, with a related pick-up of orders after September 18. The following table points up the similarities between the movements of import quantities and prices

1/ Estimates based on Department of Commerce quantity and unit value indexes.

on the one hand and of business activity and domestic prices on the other. The underlying relationship between manufacturing production (the index for which is given in column 1) and import quantities is not necessarily a direct one: it might be said more correctly that both are influenced in varying degrees by similar forces.

Table 2

Indexes of Manufacturing Production, Wholesale Prices
and Import Quantities, Prices and Values

1948-50
(1948 = 100)

Period	Fed. Res. Index of Manf. Prod. (seasonally adjusted)	Commerce Dept. Import Quantities	Indexes ^{1/} Import Unit Values	BLS Wholesale Price Index	Index of Import Values
<u>1948</u>					
I	101.3	102.8	97.7	98.5	100.5
II	99.2	95.0	99.2	99.5	95.1
III	98.7	97.9	101.5	102.4	98.9
IV	101.3	104.3	100.8	99.3	105.9
<u>1949</u>					
I	98.7	99.3	100.0	96.3	99.5
II	90.2	94.3	94.7	94.3	89.7
III	89.2	90.8	93.2	92.9	84.9
IV	91.2	106.4	92.4	91.9	98.9
<u>1950</u>					
I	97.2	111.3 (113.9)	94.7 (88.2)	92.2	105.9 (100.9)
April	99.7	100.0	96.2	92.6	96.8

^{1/} Indexes based on imports for consumption. Not seasonally adjusted. The April quantities are probably seasonally low. First quarter figures in parentheses relate to total imports excluding coffee.

A striking thing about the comparison shown in columns 1 and 2 of Table 2 is that import quantities, after falling along with business activity in the United States in 1949, rose considerably more than manufacturing production in the fourth quarter of 1949 and the first quarter of 1950. Part of this difference may be ascribed to the more rapid recovery in the nondurable industries which are more important consumers of imported materials. Another part may be due to an increased rate of Government stockpiling. There were some seasonal increases in food imports from mid-1949 to early 1950. The quantity of imports of finished manufactures rose along with other imports, and to some extent this may have been a result of improved marketing conditions following devaluation. The dollar amount of the increase in imports of manufactured goods, however, was small in the total picture.

Composition of Imports in 1950 Compared with 1948.— While the value of imports in the first quarter of 1950 surpassed the 1948 average and was about equal to the peak fourth quarter of 1948, the quantity (with price changes eliminated) was at an all-time high, 7 percent above the fourth quarter of 1948 and 11 percent above the 1948 average. (See Table 2, columns 5 and 2.) This net increase in the real volume of imports between two periods of high activity and demand appears to have been widely distributed among the various categories of imports. (See Table 3, next to last column.) Some part of the difference between import quantities in the first quarter of 1950 and the average for 1948 can be ascribed to seasonal influences. First-quarter imports of wool and of many crude foods (including cocoa and vegetables) are likely to exceed the quarterly average for the year. On the other hand, the quantity of coffee imported, which would ordinarily be seasonally high in the first quarter as well as in the last quarter of the year, was sharply reduced in January-March 1950 to below the 1948 average.

On a value basis, the net increase of quarterly imports between the 1948 average and the first quarter of 1950 is more than fully accounted for by increases in the value of coffee, wool and petroleum imports. (See Table 3.) The net rise in the value of coffee imports is wholly due to the recent sharp advance in coffee prices. The wool increase, as already noted, was partly seasonal, but it was magnified by a 15 percent rise in prices. Petroleum prices were unchanged. The increase in volume of petroleum imports continued a trend experienced since 1946. Possibly this differential upward trend of petroleum imports, as compared with total import quantities, may already have been halted by action of the importing companies in response to pressures from independent oil producers and union labor in coal mining.

The decrease in the value of other imports since 1948 shown by the first-quarter statistics is due mainly to price decreases. (See Table 3.) Quantity increases appear to have been fairly general between the year 1948 and the first quarter of 1950. The 28 percent net increase in quantity of miscellaneous foodstuffs shown in Table 3 is due to certain crude foods (such as cocoa, tea, cattle and vegetables) rather than to "manufactured foods." Part of this change is seasonal.

General Prospects for Imports.— In one respect, the comparison of first-quarter import quantities with those of 1948 does not fully reflect the underlying strength of present U.S. import demands. Throughout the year 1948, business inventories were being increased, the aggregate expansion for the year being \$6.5 billion (constant-price basis of valuation). This growth of inventories doubtless contributed to import demands. In the first quarter of 1950, although the inventory purchase-and-liquidation cycle had passed its maximum-liquidation phase several months earlier, the rate of addition to business inventories was still only \$1.7 billion (annual rate). The price advances which occurred in spot markets for many basic commodities in April and May (including particularly sharp advances for rubber, cocoa, wool and non-ferrous metals) are a symptom that the inventory cycle is still in its rising phase. They point to the probability that import values will rise

Table 3

U.S. Imports for Consumption
(values in millions of dollars)

Items	Quarterly Averages			First Quarter April 1950	Change from Quarterly Average 1948 to 1st. Quarter 1950					
	1923-25	1936-38	1947		1948	1949	1950	Percentage Quantity 1/ Price 1/		
	1948	1948	1948		1948	1948				
Coffee	60	35	150	174	262	64	+ 88	+51	- 5	+59
Sugar	83	38	103	78	87	30	+ 8	+11	+ 8	+ 2
Other foodstuffs	88	107	166	248	258	77	+ 10	+ 4	+28	+18
Newsprint	25	27	86	103	102	34	- 1	- 1	+ 1	- 2
Wool	30	14	52	77	104	28	+ 27	+35	+17	+15
Rubber	66	45	81	78	62	30	- 16	-21	- 6	-15
Crude petroleum	17	5	40	71	95	30	+ 24	+34	+35	- 1
Gas oil & fuel oil	7	5	21	32	45	16	+ 14	+44)	+15 4/	-18 4/
Copper, tin, nickel & ores 2/	54	39	82	122	128	27	+ 6	+ 5)		
Other materials 3/	389	216	583	598	539	171	- 59	-10)		
Other finished mfrs. 5/	150	84	133	189	190	65	+ 1	+ 1	+ 9	- 9
Total	969	615	1,411	1,770	1,872	572	+102	+ 6	+11	- 5

1/ For groups that differ from the standard Commerce Department groups, price and quantity changes have been calculated, approximately, by treating the Commerce group indexes (shifted to the base 1948 = 100) as if each were a weighted average of quantity or price relatives for specific commodities listed in this table and of an index for the residual of the group, the weights for quantity indexes being arithmetic averages of poqo and plqo, and for the price indexes arithmetic averages of poqo and poql.

2/ Includes all nonferrous ores.

3/ All "crude materials" and "semi-manufactures" not included elsewhere, plus burlap.

4/ Suitable quantity and unit value measures are not available for gas oil and fuel oil (the values of which are not published separately from each other) nor for nonferrous ores. The indexes shown in the tables relate to the three bracketed groups combined.

5/ "Finished manufactures" minus newsprint and burlap.

further during 1950, if only as a reflection of higher prices. Possibly import quantities will also continue to rise. The fact that imports dropped in April below the first-quarter level is not of great significance, since the 1948 and 1949 records both show temporary drops in April.

In assessing the likelihood of further general increases in import quantities during or immediately after the boom phase of the inventory cycle, consideration should be given to supply availabilities in the exporting countries and to competing foreign import demands, and also to possible variations in the rate of U.S. stockpile purchases of such commodities as metals and rubber. For some time ahead, another matter of interest will be the extent to which U.S. imports of manufactured goods may rise as a result of changes in international competitive positions brought about by the devaluations.

Exports

Over the past two or three years there have been substantial changes in the composition of U.S. exports. It is generally known, for example, that the value of foodstuff exports has fallen more than proportionately to total export sales. To identify some of the other significant changes we must go beyond the usual broad economic classifications of exports. (See Table 4.)

There has been one striking exception to the general rule that exports have declined. This is raw cotton. Since the middle of 1948, cotton exports have shown a marked upward trend, and the volume this year for the first time since the war is comparable with prewar. The monthly and quarterly figures have fluctuated widely, perhaps partly because much of the cotton sold has been financed through ERP and other aid programs. In the first quarter of 1950 the value of cotton exports was more than double the amount in the corresponding period two years before, which in turn was approximately average for the calendar year 1948. On an annual basis, the increase has been from about \$500 million to \$1.2 billion. Probably this high rate in the first quarter will not be sustained throughout 1950. Nevertheless, since supplies of cotton outside the United States are insufficient to meet consumption in foreign countries, U.S. exports are likely to remain fairly large during the remainder of this crop year (ending with July) and perhaps also in the next crop year. The growth of cotton export values has reflected a rise in tonnage shipped. Cotton export prices in the first quarter were 7 percent below the 1948 average level.

Apart from raw cotton, the annual rate of U.S. exports of domestic merchandise in the first quarter of 1950 was \$8.2 billion. This was 32 percent below the 1948 figure of \$12.0 billion.

Among individual commodities and minor commodity groups accounting for this decline, three stand out with special significance: coal, cotton manufactures, and automobiles, trucks and busses. In 1948, these items had already begun to shrink faster than U.S. exports generally, but they still accounted for 12-1/2 percent of all exports. The relative

Table 4

U.S. Exports of Domestic Merchandise
(values in millions of dollars)

Items	Quarterly Averages			First Quarter April 1950	Change from Quarterly Average 1948 to 1st. Quarter 1950					
	1923-25	1936-38	1947		1948	1949	1950	Dollar Value	Percentage Changes Quantity / Price 1/	
	80	107	128		301	79	79			
Raw cotton	235	80	107	128	301	79	+173	+136	+152	- 7
Total, other than raw cotton	882	651	3,684	3,005	2,058	720	-947	- 32-	- 22	-13
Coal	32	15	155	120	25	22	- 95	- 79	- 83	+21
Cotton manufactures	30	10	191	114	47	20	- 67	- 59	- 49	-24
Autos, trucks and busses	39	72	195	157	74	23	- 83	- 53	- 52	- 1
	101	97	541	391	146	65	-245	- 63		
Crude foodstuffs	81	34	337	317	200	66	-117	- 37	- 20	-21
Wheat flour	22	5	152	121	22	9	- 99	- 81	- 73	-31
Other mfrd. foods	129	37	287	208	119	45	- 89	- 43	- 21	-28
	232	76	776	646	341	120	-305	- 47		
Iron and steel 2/	39	61	273	214	156	51	- 58	- 27)		
Machinery 3/	82	108	580	561	483	164	- 78	- 14)		
Merchant vessels	--	--	156	64	51	13	- 13	- 20)		
All others	428	309	1,358	1,129	881	307	-248	- 22)		
	549	478	2,367	1,968	1,571	535	-397	- 20	- 12	- 9
Total	1,117	731	3,791	3,133	2,359	799	-774	- 25	- 15	-11

1/ See footnote 1 to Table 3.

2/ Includes iron and steel semi-manufactures, steel mill manufactures and iron and steel advanced manufactures.

3/ Includes electrical machinery and apparatus, industrial machinery, office appliances, agricultural machinery and implements, tractors, and tractor parts and accessories.

decline in exports of these products continued in 1949 and by the first quarter of 1950 they formed only 6 percent of total exports. Evidently increased production abroad, import restrictions and the working off of post-war backlogs of demand have operated to bring exports of coal, cotton textiles and autos and trucks down to levels which may prove more nearly sustainable. The recovery of U.S. raw cotton exports has of course facilitated the recovery of cotton textile production abroad. The January-April monthly figures suggest that the decline in U.S. exports of these products has now ended except possibly for passenger automobiles.

The items discussed in the preceding paragraph account for more than one-fourth of the \$3.8 billion decrease since 1948 in the annual rate of exports other than raw cotton. As Table 4 shows, an even larger fraction of the decrease is to be found in the foodstuffs group. In the case of foods, a significant part of the decline in value is due to the price factor.

Among foodstuffs, the decline has been particularly great for wheat flour, the exports of which have fallen continuously quarter by quarter since the middle of 1947. Flour exports, however, should be considered in conjunction with exports of grain. The "crude foodstuffs" group (including all grains, as well as fresh and dried vegetables, fresh and frozen fruits, peanuts and some other minor items), when broadened to include wheat flour, shows a 51 percent decrease from the quarterly average of 1948 to the first quarter of 1950. Within the group, fruits are the only exception to the general rule of decreases $\frac{1}{2}$. The decline of "manufactured foodstuff" exports, other than flour, has been almost as large, amounting to 43 percent between 1948 and the first quarter of 1950. In this group, which includes dairy products, lard, other meat products, rice, canned vegetables and dried fruits, there have been divergent movements. Lard exports have been well sustained because of the continuing world shortage of vegetable oils.

The pattern of almost continuous decline over a three-year period which has characterized U.S. exports of coal, cotton textiles and automobiles from mid-1947 to early 1950 does not apply to U.S. exports in general nor to foodstuffs in particular. For most exports the inauguration of the Marshall Plan in mid-1948 arrested the earlier downtrend and led to secondary post-war peaks in U.S. export quantities. The secondary peak occurred for crude foods plus flour in the first quarter of 1949 and for other manufactured foods in the second quarter. Consequently comparisons of the quantity of U.S. exports of foodstuffs in 1950 against 1948 do not indicate the full magnitude of the decline in volume which occurred during the latter half of 1949.

1/ Corn exports have also been larger than in 1948. This does not reflect a true trend, but is due rather to the exceptionally small U.S. crop of this particular commodity in 1947 and the consequently small exports in 1948.

A special characteristic of food exports from mid-1948 to the end of 1949 was the sharply downward movement of unit values (prices). Because of this fall in food prices, the increased quantity of food exports in the first half of 1949 cost foreign buyers no more than their purchases from the United States in the second half of 1948. Then, when the volume fell off again in the latter half of 1949, the decline in prices magnified the drop in values. The net result, comparing the first quarter of 1950 with the year 1948, has been that while total food-stuff export values have fallen by 49 percent, the quantity (or value at constant prices) has fallen only about 30 percent below 1948.

This decrease in U.S. exports of foodstuffs is related to a real improvement in Europe's food supply position. Good crops in Western Europe in the past two seasons, together with heavy European imports, have rebuilt that area's stocks of grain. Thus Europe's requirements for outside supplies during the current crop consumption year will remain substantially below the requirements of a year or two ago. Moreover, the outlook for the coming crops in Europe is good.

Decreases since 1948 in other U.S. exports (including some crude materials, but chiefly manufactured and semi-manufactured products) account for only \$1.6 billion of the total decline. In percentage terms, this fall has been relatively small since the total amounts involved are very large, amounting to \$7.9 billion in 1948 and \$6.3 billion (annual rate) in the first quarter of 1950. For machinery exports the drop in value has been only 14 percent. For all other exports it has been 23 percent. Since prices have generally declined moderately since 1948, the over-all quantity decrease for this grand residual of U.S. exports, including machinery, is apparently somewhere between 10 and 15 percent.

General prospects for exports.— Several considerations point to the unlikelihood of a large rise in the value of U.S. exports during 1950 despite generally strong underlying conditions of demands abroad. (1) Competition with European products in third markets will tend to minimize price increases on exports of U.S. manufactures. (2) It is doubtful whether machinery exports, which have thus far been better sustained than other U.S. exports, will increase appreciably. European production of capital goods is continuing to grow. Moreover, no notable expansion in the flow of loan and equity capital to South America, Asia and Africa can be foreseen for the immediate future. (3) Although ERP countries are likely to get a considerable increase in their gold and dollar reserves during 1950, they will tend to regard the additional reserves as a necessary protection against possible future deficits after ERP aid will have fallen off in 1951 and ended in 1952. The ERP countries will probably not relax significantly their restrictions against imports from the United States during 1950.

It might be expected that countries gaining dollar income from the increase in U.S. imports of raw materials and foods since last year would enlarge their purchases from the United States, and this will undoubtedly happen in many cases. For a variety of reasons, however, it is possible that increased import demands in these countries may not produce

a proportionate rise in U.S. exports to them, and in some cases there may be no increase at all. In those Latin American countries where trade is relatively free from currency-discriminatory controls because trade payments and receipts are chiefly in dollars, European exporters may be able to obtain a growing share of the market. In many other countries, in Latin America and elsewhere, dollar imports are subject to severe restrictive controls, some of which were tightened in 1949. Even with a marked increase in dollar receipts, the relaxation of such discriminatory controls is likely to be a gradual process until reserve positions have been substantially improved. In some cases, dollar income in 1950 may be insufficient -- given the existing rate of purchases from the United States -- to eliminate a drain on dollar reserves or the drawings of a sterling area country on the central dollar pool held by London. In other cases, countries gaining dollar income from sales of materials and foodstuffs may wish to devote part of the increment to repaying current arrearages, to rebuilding dollar reserves, or to increasing their contributions to the sterling area dollar pool. In still other cases, where we might look for a relaxation of controls over dollar imports in consequence of an easing of the dollar reserve shortage, Europe's trade with independent-currency countries may sooner or later produce net balances in favor of Europe and eventually there may be an increasing tendency to use dollars to settle such bilateral balances.

A later article will analyze the distribution among foreign countries of the recent change in the U.S. export surplus.

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REPRESSED INFLATION IN NORWAY

Paul Gekker

Ever since the German currency reform, Norway has been the European country in which "repressed inflation" has been the most pronounced. Although there has been a reduction of inflationary pressure since the end of the war, the persistence of an inflationary potential is unmistakable and has an important bearing on Norway's economic recovery and external viability.

War damage in Norway was one of the most severe of any country in Europe. It is estimated that Norway lost one-fifth of its real wealth; wide areas in the northern provinces were left devastated, and over half the merchant fleet was lost. Norway's need for housing was most urgent, and its economy suffered from acute shortages of goods of every sort.

The magnitude of the task of reconstruction justified the adoption of an aggressive program designed to make good these losses. The central feature of that program was an ambitious investment plan, which called for the highest ratio of investment to national income in Europe. The requirements of the investment plans - directed to the reconstruction of war-damaged productive capacity, especially for export, the replacement of shipping losses, and the construction of badly needed housing - have guided every decision of policy taken since its adoption. Thus, despite an increase in population, consumption still remains below prewar. In addition, some investment was directed to expanding "foreign exchange-saving" industries in order to reduce dependence upon imports of consumers' goods. At the same time, there was some attempt to expand long-deferred communal needs, and to provide for new schools, municipal buildings, hospitals, roads and the like.

Monetary background and developments

After liberation, a real limitation to the successful implementation of the investment program was the existence of serious latent inflationary pressures. As indicated in table 1, which shows the major changes in the money supply and its components, this inflationary pressure arose in the first instance from the expansion of means of payment as a direct result of the German exploitation of the Norwegian economy.

Table 1

Items	1939		1945		1946		1949	
	Mill Kr	Index	Mill Kr	Index	Mill Kr	Index	Mill Kr	Index
Currency	544	100	1700	313	1866	343	2250	414
Demand deposits	205	100	2948	1438	2398	1170	2564	1251
Total Money	749	100	4648	621	4264	569	4814	643
Supply								
Time deposits	2706	100	4708	174	4862	180	5798	214
Wholesale prices		100 ^{1/}		143		148		161

^{1/} In 1939 wholesale prices had risen by 16.3 per cent with respect to the previous year.

Source: International Monetary Fund, International Financial Statistics, and Norges Bank Bulletin.

At the end of 1945 total currency and demand deposits was more than six times as much as in December 1939. The outstanding characteristic of this expansion, however, was the growth in demand deposits. Although the note circulation tripled from December 1939 to December 1945, deposits in current accounts were over fourteen times larger. Savings deposits, on the other hand, had not quite doubled by the end of 1945. In consequence, the ratio of demand to total deposits rose from 7 per cent to 38.5 per cent in the same period.

In common with a number of other European countries, Norway made an early attempt to reduce the total volume of liquid funds. The currency reform of September 1945 combined an exchange of notes with a partial blocking of bank deposits. These measures, however, did not lead to any significant reduction in the money supply. Prior to conversion, substantial amounts of notes were turned into the banks resulting in a shift from currency to deposits. In the period immediately following the reform a considerable portion of blocked deposits was in turn released.

For the period from December 1939 to December 1945, the two significant developments were the very large increase in demand deposits and the decline in private loans. Both of these phenomena relate to the cessation of much of the normal activity during the period of the German occupation. The expansion in cash holdings, reflected in the growth in demand deposits, resulted from a combination of increased incomes from the expenditures by the occupying authorities, the accumulation of business reserve funds, and the depletion of inventories. The resulting liquidity, together with the virtual stagnation of the business and industrial community, in turn explains the decline in the amount of private credits granted. As a result of these changes, the ratio of short-term loans and advances to deposits fell from 63 per cent at the end of 1939 to 12 per cent in December 1945. The principal asset and liability items of the Norwegian private banks are shown in Table 2.

The decline in private credits during this period was offset by an increase in holdings of Government securities, which rose to almost eight times the prewar total. The major portion of these earning assets were Treasury bills, issued during the occupation period to finance Government expenditures. In addition bank holdings of long-term Government securities also increased, while investments in the obligations of other official agencies declined slightly. In the shift from private to public earning assets, Government credits, which were equal to only one-quarter of private credits in December 1939, had increased to slightly more than three times the volume of private credits by the end of 1945, and the ratio of Government to total credits rose from 20.5 per cent to 75.5 per cent during the same period.

The rise in demand deposits by more than fourteen times the total for December 1939 was in comparison to only a ten-fold expansion of the banks' cash reserves. As a result of this change the liquidity ratio was reduced from 41 per cent at the end of 1939 to 28 per cent in December 1945.

Table 2

Norway - Private Bank Assets and Liabilities
(end of year figures)

	1939	1945	1946	1947	1948	1949
	Mill Kr	Mill Kr	Mill Kr	Mill Kr	Mill Kr	Mill Kr
<u>Assets</u>						
Cash and Norges Bank deposits	83.9	823.2	887.3	1442.8	979.1	1504.9
Credits to Government:	721.4	5695.8	4505.3	3689.7	3665.6	2724.0
Treasury bills	-	4173.9	3007.6	1718.7	1581.1	433.3
Gov securities	268.2	1125.0	1076.9	1548.2	1521.8	1551.6
Other Government ^{1/}	453.2	396.9	420.8	422.8	562.7	739.1
Private credits: ^{2/}	2802.1	1852.1	2850.7	3825.8	4614.3	5259.4
Securities	170.1	229.4	394.4	486.8	535.9	605.5
Loans and advances	1845.6	934.1	1574.9	2243.9	2755.5	3044.8
Mortgages	786.4	688.6	881.4	1095.1	1322.9	1609.1
<u>Deposit Liabilities</u>	2911.3	7655.9	7259.6	7857.6	8189.2	8361.9
Demand deposits	205.0	2948.0	2398.0	2742.1	2736.5	2563.5
Time deposits	2706.3	4707.9	4861.6	5115.5	5452.7	5798.4

^{1/}Obligations of central Government.

^{2/}Obligations of other official entities (State banks, municipalities, etc.)

Source: Data furnished by International Monetary Fund.

Since the end of 1945 there has been a steady increase in private lending, both for the financing of capital investment and for construction, as well as for an increased scale of ordinary commercial activities. Nevertheless, the prewar proportion of ordinary loans and discounts to total credits has not yet been reestablished, so that security holdings and mortgage loans occupy a more important place. In 1939 discounts and advances accounted for 52.4 per cent of total credits, while securities and mortgages combined comprised 47.6 per cent; at the end of 1949, however, these ratios were 40.3 and 59.7 per cent, respectively. This shift in the composition of loans reflects the decline in short-term advances and the increase in holdings of Government long-term securities, as well as the expansion of mortgage loans to finance construction activities.

Supplementing these indications of the shift in the composition of loans, Table 3 shows the annual rate of increase by category of loan for the period 1946-1949. Following a significant increase in lending activity in 1946, the annual rate of increase for all loans declined steadily during the following three years. While the expansion of security holdings and of short-term private lending shows considerable reduction over the four-year period, the movements in mortgage credits exhibit an almost steady rate of increase from year to year as a result of the continued strong expansion of construction.

Table 3

Norway - Expansion of Credit, 1946-1949
(annual rate of increase, from
year-end figures)

	1946	1947	1948	1949
	(in percent)			
Domestic credits				
Securities ^{1/}	+72	+23	+10	+13
Loans and advances	+69	+42	+23	+11
Mortgages	+28	+24	+21	+22
Rate of increase, all categories	+54	+34	+21	+14

^{1/}Total of all Government and private issues, but exclusive of Treasury bills.

Source: Data furnished by International Monetary Fund.

In the course of 1949 there was a further increase in loans against mortgages and securities, indicating the part played in feeding the credit expansion by construction and investment projects. For the first time since the end of the war, however, total earning assets of the banks decreased in consequence of the Government's policy of no longer renewing Treasury bills. The reduction in Treasury bills by 1148.1 million kroner has brought the banking system a step nearer a normal structure with respect to earning assets and thus moderates somewhat the feeling of monetary ease generally associated with large holdings of these near-liquid assets. Only a portion of the proceeds from the sale of Treasury bills, or 851.3 million kroner, was used for further credit expansion. Thus in the course of the liquidation process, the banks accumulated cash which in the immediate future constitutes an available resource for further credit expansion. The addition to cash reserves increased the liquidity ratio from 35.8 to 58.7 per cent.

The joint stock bank laws provide that reserves equal to 25 per cent of demand liabilities and 5 per cent of total liabilities be kept in the form of cash and central bank deposits, plus so-called "liquid means," which is defined to include Treasury bills, certain obligations of Government institutions, and foreign balances. This ratio for savings banks must equal 10 per cent of total deposits. With reserves taken to mean cash, central bank deposits, and Treasury bills, reserve requirements for the banks would be roughly fulfilled if these totalled NKr. 1098 million on December 31, 1949. As of that date these items amounted to NKr. 1933 million, and therefore present reserve requirements do not constitute an effective limit on the ability of the banks to expand credit.

The claims of the private banks on the central bank are clearly potentially inflationary. At present the only check to a further rapid expansion of credit seems to be the extent to which the banks cooperate in the selective policy recommended by the Bank of Norway. However, under a unit banking system such as

Norway's, the difficulties of administering credit controls are increased because of the vulnerability of isolated banks to local pressure for credit accommodation. The fact that the credit request is quite legitimate in relation to the local need only fortifies the argument for some quantitative control which would set lower limits on the expansion of credit which is still possible at the present level of bank reserves. 1/

Internal aspects of repressed inflation

The preceding paragraphs review certain initial causes and reasons for the continuation of repressed inflation in Norway. One proof of the persistence of the familiar manifestations of these monetary conditions is that today, five years after the end of hostilities, it still is not possible to relax any of the strict controls which perpetuate these same tendencies. A recent disappointing example of this was the removal of cement rationing, which had to be reimposed because supposedly ample supplies in the summer of 1949 called forth a demand for building materials for repairs, chiefly by small users, which greatly exceeded expectations. According to the Norwegian Road Directorate, despite an increase in the tax on gasoline, the elimination of driving restrictions in June 1949 led to a 7 per cent increase in the consumption of gasoline by March 1950. It has also proven impossible to ease restrictions on foreign travel by increasing the amount of currency permitted the Norwegian traveller because of the threat that the drain from such expenditures would reach unmanageable proportions.

In Norway, the mechanism of control is very comprehensive, combining price control, rationing and allocation devices, and exchange and import restrictions. The entire system of controls is considered necessary because of the automatic link between wages and movements of the cost-of-living index, which makes it imperative to hold price fluctuations within a very narrow range. The index has been stabilized since the end of 1945 by the payment of subsidies on a number of important commodities. These outlays have increased in each fiscal year since their adoption. Only the likelihood that the September 1949 devaluation would necessitate a scale of subsidies impossible to finance through new taxation, led to the decision to limit these payments to Nkr. 600 million in the coming fiscal year.

Price control and rationing have prevented the inflated purchasing power from becoming an effective demand for goods not immediately available because of the policy of concentrating on the most urgent tasks of reconstruction. The fact that the postwar increase in wholesale prices, shown in Table 4, has been limited to approximately 13 per cent, is partial evidence of the considerable success of this system of controls.

Table 4

Norway - Price Indices (1938 = 100)

	End of 1939	End of 1945	End of 1948	End of 1949
Wholesale price index	116.3	166.0	182.6	187.1
Cost-of-living index	106.8	156.3	157.3	158.9

Source: Norges Bank Bulletin, No. 1, 1950.

1/ See remarks by Governor Jahn, in his annual address to the Supervisory Council of the Bank of Norway, reprinted in Norges Bank Bulletin, Feb. 22, 1949, pp.11-12.

Under conditions of relative price stability, coupled with the virtual absence of labor disputes, a fairly uninterrupted expansion of output has taken place. The progress of production shown in Table 5, however, illustrates another effect of repressed inflation. From 1945 on, the index of industrial production has risen from lower than prewar to some 40 per cent above the 1938 level, but recovery has lagged seriously behind in the industries producing for export. The principal explanation for this development is that a larger than prewar portion of increased output is diverted to home use, partly to satisfy consumer wants, partly to meet some requirements of the reconstruction program.

Table 5

Annual averages	Norway - Indices of Industrial Production (1938 = 100)					
	1939	1945	1946	1947	1948	1949
All industries	106.6	68.9	100.4	115.0	124.9	132.0
Export industries	103.3	44.5	68.4	82.0	92.3	109.6
Domestic industries	108.1	80.7	115.7	130.9	140.6	142.8

Source: Norges Bank Bulletin.

One indication of this greater domestic use of industrial output is a comparison between the prewar and postwar shares of production which went into exports. The Norwegian Statistical Bureau has calculated the "export shares" of production for a number of industries, and some of these are reproduced in Table 6. In a few instances this proportion is above prewar, but for all industries surveyed by the Bureau the average figure for the proportion of industrial output exported was 58.1 per cent in the first half of 1949, against 65.3 per cent in 1938.

Table 6

Norway - Exports as Percentages of Industrial Output

Industries	1938	1948	Jan. - June 1949
Ores:	82.5	65.0	53.2
Iron ores	101.5	63.5	38.0
Pyrites	63.7	66.4	61.9
Forest Products:	62.5	50.7	50.5
Pulp	57.3	45.6	53.8
Cellulose	56.8	35.2	40.6
Paper	75.5	69.7	64.6
Cardboard and carton	39.7	27.8	15.4
Metals	85.5	81.2	79.8
Electro-chemical products	91.0	78.8	96.0

Source: Norges Offisielle Statistikk, Okonomisk Utsyn over Aret 1949, p. 61.

Moreover, the pressures of this increased domestic demand has not been counteracted by a wage policy which would introduce a differential in favor of occupations in export industries presumably because of the dangers of such a policy for wage stability in general. This further evidence of repressed inflation is attributable to the present favorable relationship between wages and prices. The rough calculations summarized in Table 7 below indicate that in the postwar period money wages have risen more than the cost-of-living and as a consequence real wages are now higher than prewar.

Table 7

Norway - Money Wages, Cost-of-Living,
and Real Wages
(1938 = 100)

Year	Indices of Average Hourly Earnings				Cost of Living (5)	Real Wages	
	Male (1)	Female (2)	Skilled (3)	Unskilled (4)		Male (6)	Female (7)
1938	100	100	100	100	100	100	100
1945	133	136	117	120	155	96	88
1948	180	195	158	170	158	114	123
1949	191	204	169	194	157	120	129

Computed from Statistiske Meldinger, 1950, No. 4, Tables 43 and 44, pp. 39-40. Index of real wages calculated for columns (1) and (2) only.

The pattern of this development in wages is also due in part to the policy designed to assure a more socially desirable equalization of incomes. The differential between skilled and unskilled wage rates has been narrowed, which suggests the possibility that productivity has suffered from the removal of individual incentives and by a reduction in the mobility of labor. The most recent material shows that productivity in the first quarter of 1949 was still 6 per cent below prewar (1935 - 1938 = 100). ^{1/}

There are some other indications of the internal effects of repressed inflation in Norway, but the available evidence does not make it possible to form any significant conclusions. For example, it is not possible to measure the extent of absenteeism, but its existence and the serious problem it presents is indicated by official Norwegian pronouncements pointing out the necessity of reducing to a minimum the number of working days lost. ^{2/} Another manifestation of repressed inflation in Norway is reflected in the inevitable shift in consumption in favor of unrationed goods and services, and the associated diversion of some resources to the satisfaction of these altered demands. However, with the improved supply of goods in the last year, some abatement of this tendency

^{1/} United Nations, Economic Survey of Europe in 1949, Table 4. This, as well as earlier similar references, is labelled "wrong or misleading" in the General Memorandum on the 1950-51 and 1951-52 Programmes, Paris, April 1950, p. 6. and contrary data are given in Nasjonalbudsjettet 1950, (St. meld. nr. 1), p. 116. The basis for the conflicting statements is not known.

^{2/} National Budget 1950 (English translation, ECA Mission to Norway, p. 49).

is evidenced by the decrease in sales of radios and furniture, the drop in the volume of movie tickets sold, the decrease in sales of tobacco and the decline in turnover of the Government wine monopoly. 1/

However, the most important aspect of repressed inflationary conditions is the distortion in the labor market. The failure of production for export to match the recovery in other fields is probably attributable to the consequences of repressed inflation for the distribution of labor, and this introduces the consideration of the external effects of excessive internal demand.

External effects of repressed inflation

The reverse of apparent domestic stability, evidenced by the development of prices, employment and output, has been a persistent disequilibrium in the balance of payments. This imbalance is the result of a deficit which in each postwar year has involved a constant drain in excess of forecasts and has been covered by the use of loans and bilateral credits, ECA aid, and the utilization of foreign exchange holdings. It may be noted that on a per capita basis, net aid (dollars plus drawing rights) to Norway for 1949/50 was the highest in Europe.

The postwar import surpluses are a consequence of the ambitious investment program, the primary objective of which has been the reconstruction of the Norwegian economy. Together with the task of reconstruction has also gone the aim of providing for more rapid basic development of the economy through the exploitation of unutilized (natural) water resources. The size of these import surpluses, which are in the order of 1 billion kroner for each of the last three years, is partly related to the previous references to the lag in the recovery of exports. A final factor is the failure of the shipping sector to contribute a larger share of foreign exchange earnings. During the war, very nearly one-half of the merchant fleet was lost. Its replacement was considered to be of paramount importance because of its contribution to the balance of payments. Before the adoption of the ERP, a reduction in imports, made necessary by virtual exhaustion of financing possibilities, was planned for 1948. Of all imports, only ships were exempt from the cuts. As a result of this emphasis, the merchant fleet has now been restored to slightly over prewar capacity. Despite this recovery, however, freight earnings during the past two years have not kept pace with the increase in tonnage, mainly because of the disparity between import prices and freight rates.

Immediately after the war, the Norwegian authorities planned to finance the necessary import program through the use of foreign exchange reserves acquired for wartime services rendered by the fleet and in payment for ship losses, and by the use of foreign credits. By the first half of 1948, however, it was found necessary to cut planned imports because the proceeds of credits from the United States, Sweden and Canada were virtually exhausted, and foreign exchange reserves were steadily being depleted. The beginning of ECA aid permitted the recovery of import levels from a reduction to approximately 86 per cent of prewar as planned in the first half of 1948 to a realized volume 94 per cent of prewar. In the second year of ERP, moreover, the 41 per cent increase in aid over Norway's allotment for 1948/49, when most of the participating countries' aid was reduced, was both a recognition of Norway's dependence upon external assistance and an endorsement of the Norwegian recovery program with its emphasis on large-scale investment.

1/Ibid., pp. 277-280.

Table 8

Norway - Volume Indices of Imports and Exports
(1938 = 100)

Year	Import Volume		Export Volume
	Total	Exclusive of Ships	
1946	79	78	61
1947	118	104	81
1948	100	94	81
1949	117	107 ^{1/}	84

^{1/} Preliminary estimate, National Budget 1950.

Source: Statistisk Arbok 1949; Norges Bank Bulletin,
No. 1. 1950

Table 9

Norway - Balance of Payments Financing

Items	1948		1949		1950 ^{1/}	
	Mill Kr (Percent)		Mill Kr (Percent)		Mill Kr (Percent)	
Deficit on bal- ance of payments	923	100.0	1383	100.0	1289	100.0
Financing:						
ERP	266	28.8	766	55.4	1055	81.8
Use of foreign exchange	316	34.2	279	20.2	164	12.7
Utilization of credits	159	17.2	40	2.9	-	-
Borrowing on ship imports	103	11.2	111	8.0	44	3.4
Other	79	8.6	187	13.5	26	2.0

^{1/} Forecast. Percentage details do not total due to rounding.

Source: Nasjonalsbudsjettet 1950, (St. meld. Nr. 1), p. 53.

The foregoing tabulation illustrates the extent to which ERP aid has made possible the continuation of so large an import surplus by providing for an increasing portion of the external financing for the period 1948-1950. The projected aid for 1950, showing an increase over aid in 1949, is explained by the lag between the aid authorization and its actual utilization, despite the fact that aid totals are to taper off in the remaining period of the Marshall Plan.

Even with the increased importance of ERP aid in 1949, however, other means of financing had to be used to finance the balance of payments deficit. In 1949 it was planned to cover a balance of payments deficit of 1121 million kroner by borrowing on ship imports to the extent of 266 million kroner and by the use of foreign exchange reserves in the amount of 62 million kroner in addition to ERP aid and other capital income. Table 10, showing the balance of payments deficit and its financing, compares the 1949 forecast with the results for that year.

Table 10

Norway - External Financing, 1949

	1949 (Mill Kr)	Plan (Percent)	1949 (Mill Kr)	Result (Percent)
Balance of payments deficit	1121	100.0	1383	100.0
Financing				
ERP Utilization of credits	700	62.5	766	55.4
	40	3.6	40	2.9
Borrowing on ship imports	266	23.7	111	8.0
Use of foreign exchange	62	5.5	279	20.2
Other	53	4.7	187	13.5

Source: Nasjonalsbudsjettet 1950, (St. meld. Nr. 1), p. 10.

A 262 million kroner larger deficit in 1949 is accounted for by a combination of larger imports not offset by any increase in exports, larger ship imports, and by increased service payments arising from devaluation. The increased import deficit made necessary a much larger use of foreign exchange holdings than had been planned, and larger cash instalment payments on future ship contracts reduced the extent to which the deficit could be covered by borrowing on ship imports. Most of the increase in the last grouping represents the use of credit margins provided for in bilateral agreements.

The seriousness of this external imbalance may temporarily be disguised by the coverage of the deficit in 1950 to the extent of 82 per cent by ECA aid, but it is likely to loom very large as aid tapers off. Very little further borrowing on ship imports appears to be possible, and the limit in the utilization of bilateral credits probably has been reached. Most of the deficit not covered by aid is to be met by a further reduction of exchange holdings, which by the end of the current year may thus decline to the minimum level considered essential for working balances.

Summary and prospects

The two related aspects of repressed inflation covered in this paper are disequilibrium in the labor market and the serious balance of payments position. A correction of the former is a condition for improvement in the latter, and to that end some device to attract labor to the export industries appears to be necessary. This requirement is all the more essential since it is claimed that the recent devaluation can make little improvement in the external position because the output of the export industries cannot presently be expanded. Since devaluation was supposed to have eliminated any previously existing marketing difficulties, it is all the more imperative that export production be favored by all appropriate measures.

A connected problem is that of restraining the demand for less essential investment and for projects that divert resources away from those occupations that can make the best contribution to an improvement in the balance of payments situation. The difficulty of curbing these demands on a selective basis argues for the introduction of a quantitative limitation on the large existing potential for further credit expansion.

One final aspect of repressed inflation should be mentioned; this is the resistance to the recent movement in the direction of trade liberalization. Norway has not fully implemented the OEEC decisions to remove quantitative restrictions on at least 50 per cent of all private imports. One explanation for this attitude is the fear that liberalization, by disrupting the composition of the import program, would disturb investment priorities. In other words, planned investments cannot be executed if the total of consumers' goods imports is to be subject to variation. Furthermore, the replacement of domestic substitutes by imports seems to threaten the maintenance of full employment objectives by displacing labor engaged in these domestic industries. This attitude toward trade liberalization is only the most recent example that can be attributed to the repressed inflationary situation. Besides the resistance to trade liberalization, earlier discussion relating to the formation of a Scandinavian customs union failed to lead to any concrete achievement, largely because of Norway's inability to join its neighbors in common action to bring about the union. A final example is the "Uniscan" arrangement, in which Norway failed to participate to an equal degree with the other signatories in the measures adopted to liberalize certain current account payments.

Given the unsolved internal problems, the devaluation of September 1949 increased the threat of an acceleration of the inflationary process through its implications for stability of the cost-of-living index. As of devaluation, a price freeze on imported goods was ordered. However, since depleted stocks would have to be replaced later at higher prices, the measure could be no more than temporary. The tendency for import prices to rise meant that subsidies would have to be increased, an action which presupposed the possibility of raising tax rates. Taxes, however, were already at very burdensome levels.

These developments led to the recent decision to modify the subsidies on some consumer goods. Subsequent to devaluation, it was estimated that subsidies totalling NKr. 1,050 million in 1950-51 would be necessary if the cost-of-living

index were to be kept stable. Following the recent parliamentary debates on Government financial policy, the first step in an economic program outlined by the Prime Minister was taken on April 3rd when it was decided to limit subsidy expenditures to an absolute minimum of Nkr. 600 million. At the same time, the Trade Union Federation and the Employers' Association agreed that, should the cost-of-living reach or exceed 165.6 on September 15 (4.41 per cent above the March 15 level of 158.6), negotiations for a revision of the master wage agreement expiring in 1951 would be instituted.

The reduction of subsidies introduces the first change in direction of Norway's economic policy which until now has required a continuous increase in these outlays. The action, thus far reflected in an increase of approximately 8 per cent in wholesale prices and of 5 per cent in the cost-of-living index, is therefore a hopeful sign of a realization that the transition to economic balance requires the introduction of greater flexibility in the Norwegian economy. It remains to be seen whether policy in the near future will succeed in permitting some price increases, as well as some upward adjustment in individual wage-rates, while retaining the present general level of wages unchanged. In Governor Jahn's words:

" . . . the intention is not to provoke a depression with all its consequences. That must always be borne in mind. But on the other hand, people must not be made to believe that a process of financial rehabilitation can be carried out without anybody feeling it. The purpose of such an operation is to create a situation which can provide a basis for a more rational utilization of the productive resources. Undoubtedly the consequence of the transition will have to be a temporary pressure on the standard of living; and the redistribution of labour which is a part of the process of reconversion, will be a hard blow for many people.

One of the questions that we put to ourselves is the following: Will it be possible in the years to come to maintain full employment? The reply depends on what is meant by full employment. If what is meant is a situation such as the present, with insufficient labour in many activities, a situation in which every man and woman can keep the work they have now at the place where they are living, then I would answer in the negative. On the other hand, if what is meant by full employment is that there will be work available for everybody, even if there will be some unemployment in connection with the reconversion process, then I would answer that full employment can be maintained." 1/

1/ In Norges Bank Bulletin, No. 1, 1950, p. 15.