

Printed for the Cabinet. July 1949

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C.P. (49) 158

21st July, 1949

CABINET**THE DOLLAR SITUATION**

MEMORANDUM BY THE PRIME MINISTER

In E.P.C. (49) 66 of 22nd June the Chancellor of the Exchequer gave an analysis of the dollar position on the basis of such information as was available at the time.

2. I feel that my colleagues should have an opportunity of considering the latest information now available. The main facts are as follows:—

3. *The Reserves.*—Our reserves of gold and United States and Canadian dollars at 30th June amounted to £406 million compared with £471 million at 1st April, representing a decrease of £65 million during the second quarter. The decrease would, in fact, have been much larger but for the receipt in the closing days of June of considerable sums of money in the shape of reimbursements from the Economic Co-operation Administration of expenditure already incurred by us. These large receipts were the result of special measures taken by our representatives in Washington to reduce the amounts still owing to us by E.C.A. and they have been followed by a sharp reduction in further reimbursements since the beginning of July. As a result of this and of the continued heavy gold and dollar deficit, our reserves have continued to decline rapidly and by 20th July had fallen to £372 million. In other words, they have fallen by £21 million in about half a month or at a rate of over £120 million a quarter.

4. *E.R.P. Receipts.*—E.R.P. aid in all forms during the second quarter amounted to £85 million (including £8 million received by the Irish Republic) compared with £81 million in the first quarter. But for the heavy reimbursements already mentioned, the figure would have been a good deal less than in the first quarter. It is not possible to forecast with any accuracy what the total E.R.P. assistance in the third quarter is likely to be, but it can hardly be much in excess of £70 million.

5. *Gold and Dollar Deficit.*—The monthly gold and dollar deficits during the second quarter were as follows:—

	\$ million
April	149
May	228
June	255

632

(or £157 million)

The figure of £157 million is to be compared with the following quarterly deficits since E.R.P. began at the beginning of April, 1948: £107 million, £76 million, £93 million, £82 million.

6. The course of the deficit in recent weeks is shown below:—

<i>Week ending</i>	<i>\$ million</i>
4th June	62·2
11th June	48·2
18th June	53·2
25th June	71·6
2nd July	68·6
9th July	55·5
16th July (provisional)	(50·0)

The present week (ending 23rd July) will be a heavy one, as we shall have to pay \$18 million to Belgium and \$11 million to Switzerland for the settlement of the sterling area deficits with these countries in June.

7. The deficit is still, therefore, running at the rate of over \$50 million a week which is equivalent to over £600 million a year. At this rate, even if we assume that we are allotted over £200 million in E.R.P. assistance during 1949-50 and can continue to draw on the Canadian Credit on the same scale as recently (*i.e.*, \$10 million a month), the whole of our remaining reserves would disappear within about a year.

8. Some provisional details of the make-up of the sterling area gold and dollar deficit in the second quarter have been compiled and are shown in the Appendix, together with figures for the first quarter and the forecasts for the second quarter which were made early in April.

9. These estimates show that though United Kingdom purchases in the United States were larger in the second quarter than in the first, they fell a good deal short of the original forecasts. This was due partly to lack of availability of some items and partly to action which was taken to cancel purchases during the quarter.

10. United Kingdom export proceeds were not very much less than in the first quarter, but very substantially below what was expected. It should be noted that since the figures given relate to export *proceeds* they do not fully reflect the reduction in actual shipments to the United States which has taken place. These continue to decline. In June they were only £3·0 million compared with £3·7 million in May, £3·4 million in April and a monthly average of £5·8 million in the first quarter. Exports to Canada were also lower in June than in May, but very little less in the second than in the first quarter as a whole. It is too soon to say whether the drop in June denotes the beginning of a new downward trend and we shall have to watch subsequent figures with great care.

11. During the second quarter, there was a sharp deterioration in the position of the dollar invisibles. This is partly the result of unexpectedly heavy expenditure on certain items, such as dividend transfers and the outlays of British oil companies. There was also a reduction in our receipts from oil sales. Finally, a large conversion of American sterling balances took place in April and is reflected in the figures. Since April, however, these balances appear to have been reasonably stable.

12. Dependent overseas territories (D.O.T.s) and the countries in the independent rest of the sterling area (R.S.A.) all fared worse in the second quarter in comparison both with the first quarter and with our earlier expectations of the second. As far as the D.O.T.s. are concerned, this was the result primarily of a sharp reduction in United States purchases of rubber, cocoa and tin. Receipts from all colonial exports to the United States in the second quarter are provisionally estimated at \$64 million compared with \$115 million in the first quarter. The increased deficit of the independent R.S.A. countries with the United States is also, in part, the result of lower income, particularly from sales of wool and jute. But some increase in expenditure has also taken place, particularly by Pakistan.

13. Our settlements with Switzerland and Belgium were much heavier than in the first quarter, and large payments will also have to be made to both this month. There is no evidence at the moment that the position with regard to these countries is improving, and although the new intra-European payments scheme in 1949-50 should reduce the drain to Belgium, any excess in our deficit over that agreed between us in advance will still have to be met in gold.

14. Our gold losses to other countries, particularly Persia, were lower in the second quarter than in the first and even lower than we had expected. But there is no reason to believe that this is more than a temporary respite. In June the Persian loss had again increased to about \$10 million.

15. The above facts bring the story of our gold and dollar position as up to date as possible. All the evidence suggests that expenditure both by the United Kingdom and the rest of the sterling area is still on a heavy scale, and that some time must elapse before the measures taken here and those recommended to other Commonwealth Governments as the result of the Finance Ministers' Meeting can begin to take effect. Meanwhile there are few signs of any recovery in our dollar income (apart from a resumption of United States purchases of tin towards the end of June, which is the only favourable development that can be reported). Gold and dollar settlements to non-dollar countries are likely to remain high, at least until the arrangements with Belgium come into operation.

16. The general conclusion, therefore, must be that for some time ahead the current heavy deficit is likely to continue and with it a continued drain on the gold and dollar reserves. It is impossible at this stage to forecast with any assurance what the extent of this drain is likely to be over the next month or two. But it would be over-optimistic to hope that our reserves at the end of the current quarter will stand much above £300 million.

C. R. A.

10 Downing Street, S.W.1,
21st July, 1949

APPENDIX

STERLING AREA GOLD AND DOLLAR DEFICIT—FIRST AND SECOND QUARTERS 1949

	\$		
	<i>First Quarter Actual</i>	<i>Second Quarter Actual</i>	<i>Second Quarter Target April 1949</i>
<i>United States—</i>			
United Kingdom Purchases ...	-54	- 69	- 85
Exports and diamonds	18	15	27
Invisibles, capital, &c.	13	2	19
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United Kingdom deficit with United States	-23	- 52	- 39
D.O.Ts.	16	3	8
Independent R.S.A.	-27	- 39	- 21
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Sterling area with United States ...	-34	- 88	- 52
Sterling area with Canada	-34	- 34	- 28
Sterling area with United States account	- 9	- 18	- 16
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Sterling area with Dollar Area ...	-77	-140	- 96
Switzerland and Belgium	- 7	- 16	- 13
Persia, &c.	-12	- 7	- 9
Gold purchases	14	7	5
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Total Deficit	-82	-157	-113





