MEMORANDUM BY THE MINISTER OF STATE.

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Introduction.

At a meeting of the War Cabinet on the 21st December, 1943, I was invited to prepare for the Cabinet a paper focussing the issues arising out of the Washington Conversations on Article VII. These conversations covered a wide field. There were first of all discussions on currency questions, and our delegation was instructed to secure, as far as possible, the essentials of the Clearing Union. In this they were remarkably successful and I consider that the agreed statement on Currency does embody, even though it is dressed up in American terminology, the main features of our own plan. Anything less like a Gold Standard can scarcely be conceived. It provides for changes in exchange rates when a country's balance of payments makes this necessary, for a substantial provision of credit from the United States and other creditor countries, and an international organ of consultation and adjustment not predominantly under American auspices.

There were discussions on Commercial Policy. After very lengthy deliberations by Ministers and Officials alike the Cabinet agreed, last summer, that our interests would best be served by a breaking down of trade barriers of all kinds and by the widest possible degree of multilateral trade. The Delegation accordingly proceeded to Washington with an Aide-mémoire and an Outline of Proposals, approved by the Cabinet, which were handed to the Americans at the outset, and which were the basis of discussion. Here, too, there was a wide measure of agreement. The points of difference, upon which a decision will now be required, and the safeguards upon which we must insist, will be found in Annex B of this paper.

Commodity Policy formed a third topic. Here again our delegates were remarkably successful in achieving agreement with the American officials on a set of principles in full accord with our own ideas. These include, in accordance with the Cabinet decisions of last summer, the institution of a Commodity Policy...
organisation, the application of the Buffer Stock technique where that is practicable, and the use of quantitative restrictions of production or export of primary products only as a temporary measure where there is a severe maladjustment between supply and demand and with proper safeguards for the interests of consumers and efficient producers.

On the initiative of the Americans there was also a very preliminary exchange of views upon Cartel Policy and Employment Policy. The Americans also handed to our Delegation the first draft of an International Investment Bank.

The War Cabinet have already approved the general line of policy which underlies the Washington Conversations. I had hoped, therefore, that I should be able to confine myself in this paper to an examination of the extent to which the principles which were agreed at Washington conformed to Cabinet policy; and to focussing the issues upon which further decisions of policy are required in the light of the Washington talks and of the forthcoming conversations with the Dominions.

It is clear, however, that some of my colleagues wish to re-examine the whole policy outlined in Article VII of the Mutual Aid Agreement, which the War Cabinet has already approved and which was the basis of the talks in Washington last September. It seems necessary, therefore, for the War Cabinet to come now to a final decision on this matter. For if it is decided to reverse the present policy, it will be necessary so to inform the Dominions and the Americans.

I should, perhaps, add that we are not trying to agree in detail the terms of a treaty with the United States Government. We are seeking to formulate with them a set of principles which we can jointly try out on third parties, and which can be transformed into international instruments to be brought into force only gradually and over a relatively long period of years.

The Extent of our Commitment.

The Mutual Aid Agreement was signed in February 1942. Its signature was attended by many doubts and hesitations. And it was only after the most searching debate, and after the deployment of all the arguments which have recently been advanced by the Secretary of State for India and the Minister for Agriculture and Fisheries, that we agreed to sign.

"It may have been necessary," says the Secretary of State for India, "for political reasons to agree to Article VII." But the thesis that the Mutual Aid Agreement was no more than a political gesture does not bear examination. It was not an exercise in American appeasement, nor a surrender to American blackmail. No doubt a consideration which powerfully influenced the Cabinet's decision was the underlying conviction that we must march with the Americans in the economic as in the political field. But the basis of our signature of the Mutual Aid Agreement was the belief that the policies indicated in Article VII offered the most hopeful prospect of a solution of the very serious problems with which we ourselves will be faced after the war.

More than that. The three projects upon which the Washington talks were mainly centred were not American proposals to which we were being pressed to a reluctant assent. They were British projects which we, for our own purposes, were pressing upon the Americans. And we were pressing them because it became clear, as the result of prolonged and massive consideration both departmentally and in Cabinet, that the balance of advantage for us—not for the Americans or the Chinese—lay with these proposals rather than with any alternative.

All the disadvantages which must attend the signature of the Mutual Aid Agreement were canvassed at the time. It was pointed out that Article VII involved some limitation upon our absolute freedom of action, and that it impinged upon the whole system of Imperial Preference. The Cabinet decided that the advantages outweighed the disadvantages. The Mutual Aid Agreement was signed. We were henceforth committed to pursue, in co-operation with the Americans and other like-minded nations, a policy of expansionism and the removal of impediments to trade. It is not open to us, therefore, to adopt now a policy which is based upon discriminatory protectionism and the unrestricted quantitative limitation of imports.

We are committed to Article VII. Neither we nor the Americans are committed in any way to the results of the Washington Conversations. That was
clear from the start. And if we should decide, after due consideration, that the
gulf between us is so wide that it is useless to pursue any further this particular
line of approach we should be perfectly free to inform the Americans of our
decision. We would not, of course, be free to modify our general approach, for
we should still be bound by Article VII.

But we ought, I think, to be careful of how we exercise this freedom. If the
Americans had met us, while we were in Washington, on every one of the points
in our instructions, we would still be "free" to retrace our steps—so long as
we were prepared to advance again. We would not be dishonourable if we were
to overthrow our own policy. We would only look heroically silly. There must
obviously be a limit, imposed by considerations not of honour but of commonsense, to the non-committal character of non-committal conversations. As Sir Kingsley Wood pointed out in W.P. (43) 383: "We cannot regard these
discussions as an academic exercise. If our delegation reach agreement on principles with the Americans which they can recommend to us to approve provisionally for further consideration at the drafting committee, we shall be
taking the first step in a course which would lead probably to the formulation of
an agreed and detailed international scheme. This appears to me a logical and
inevitable step; if we mean anything by economic co-operation with the United
States, we must at some stage descend from generalities or pious resolutions to
more exact or difficult plans."

The issue is, therefore, whether we have in fact reached the limits of the
non-committal and whether or not the time has come to "descend from
generalities and pious resolutions to more exact and difficult plans."

II.

The American Attitude towards Article VII.

The Americans, too, are uncommitted by the Washington Conversations. To what extent are they committed by Article VII? Is it not possible that we are
tying our hands while the Americans, behind the enviable barrier of their
Constitution, retain absolute freedom of action?

Anything, no doubt, is possible under the American Constitution. Certainly
it is possible that a future Congress may repudiate the Mutual Aid Agreement.
One can never be sure, of any country, that a Government will not wriggle out
of engagements contracted by its predecessors. But what then? In freeing
themselves Congress would be freeing us. Even the Constitution of the United
States cannot free one party to an international agreement while binding the
other. And certainly we cannot get out of a solemn engagement only because
there is a chance that the other party may get out of it at some future date.
That is a reason for refusing to enter into an agreement, not for getting out
of one.

In one sense, it is true, Article VII is more binding upon us than upon the
Americans; there is a distinction between Article VII and the rest of the Mutual
Aid Agreement. Under the Lend-Lease Act the President is given irrevocable
authority to determine the benefits which the United States shall receive in
return for Lend-Lease. Article VII, however, deals among other things with
"the betterment of world-wide economic relations," and it has been argued that
this is outside the mandate which has been given to the President by the Act.
In strict constitutional theory, therefore, the first six articles of the Mutual
Aid Agreement are irrevocable, but Article VII can be held to be ultra vires of
the President and therefore revocable by Congress.

Even so, there is one passage in Article VII which appears to be
constitutional binding upon the United States, the passage which states that
the terms and conditions for the repayment of Lend-Lease "shall be such as
not to burden commerce between the two countries." And it is exceedingly
to our advantage that this should be so, for this part of the Mutual Aid Agreement
isgoing to be our sheet anchor when we come to the final settlement of Lend-Lease.

The position so far as the more general parts of Article VII are concerned
seems to be this. The declarations about the expansion of trade, the elimination
discrimination, the reduction of trade barriers and so on, are something that
the President required from us as an inducement to him to give us the advantage
of the other parts of the agreement. These declarations are binding on us and
on him but not, in the same degree, upon Congress. Congress, for its part, has
an option and it has not yet determined whether, or in what form, it will exercise it. We cannot withdraw this option. But Congress is not compelled to exercise it. Of course, if it does not exercise it, we, on our side, are equally released. But until we are released we are bound by Article VII. We must face the fact that the Americans have an option, as it were, upon sanity. Until they go mad, we for our part are under an obligation to remain sane.

There is nothing very damaging to our interests in all this. We get the invaluable advantage of terms of settlement which will not burden commerce. In addition, we have the possibility—to put it no higher—that the United States will pursue an economic policy which is very much in our interests. I do not think, therefore, that there is much force in the argument that we are bound while the Americans remain free. According to the strictest interpretation of constitutional theory we are more deeply committed than they to Article VII. But nothing would be gained if we tried to equalize matters by running out of our part of the bargain. And a very great deal would be lost.

It is said that it may be very dangerous to negotiate on matters so contentious during the Presidential year. It will certainly be impossible, it is argued, to reach an agreement during the election campaign; the effort to agree will create misunderstandings of a kind very damaging to the whole nexus of Anglo-American relations; the whole question into cold storage until this dangerous period is over? In any case, it may be said, it is likely that the present Administration will be succeeded by a Republican Administration allergic to the principles of internationalism which are implicit in Article VII; would it not be wiser, therefore, to await the result of the Presidential election before we commit ourselves irrevocably to any particular policy?

There is obviously some force in these arguments, but I do not think that they are conclusive. In American eyes it would seem to be an attempt to slip out of a commitment. And the underlying motive would not be hidden, for it would be obvious that we had drawn back because we were beginning to discount a Republican victory in November. This would not endear us to the Administration. Nor, I fancy, would it placate their opponents, who are likely to remain unimpressed by such an exercise in appeasement.

In any case it would be a mistake to base our policy upon the firm assumption that a Republican administration would be opposed, in all circumstances, to international co-operation in the economic field. The presumption is that the Republicans are economic isolationists. But it would, I think, be a mistake to wager very heavily on it. Such evidence as I have seen is scanty, but it is in the contrary sense. We have heard from Washington that the State Department have already disclosed to influential manufacturing associations the more contentious parts of the commercial policy that was agreed in Washington. The disclosure was well received, and the manufacturers, it is said, have become proselytes.

Some days ago I was talking myself to Sir Alan Anderson and Mr. Arthur Guinness, who have recently returned from a tour of the United States. They told me that the American industrialist was far more conscious than he had supposed of the straits in which he would find himself if the unduly favourable balance of payments of the United States was not adjusted by some expedient or other. Sir Alan and Mr. Guinness were firm in their conviction, it is true, that neither a drastic reduction in the tariff nor a Stabilisation Fund would be acceptable in the present state of opinion in the United States. It was clear, nevertheless, that opinion in Republican industrial circles was crystallising in this direction; something, disagreeable in greater or less degree, would have to be done to save the United States from the consequences of overwhelming economic supremacy.

It is a fact which we should be unwise, in my opinion, to ignore, that the American industrialist is nobody's fool, and that he looks as far ahead as most people. He has not forgotten that there were twelve or fifteen million unemployed in America during the depression, that this figure possesses no particular sanctity and may well be exceeded after the war, and that the social structure of the United States is not so strong that it can bear unlimited strains of this kind.

There is this further consideration. The Americans must be at least as conscious as we are of the difficulties of the Presidential election. It is a fact that the Administration are pressing us to continue the Washington Conversations. Are we wise if we refuse on account of domestic factors, not in this country, but in the United States?

I conclude, therefore, that it would be a mistake for us to desist from the policy upon which we have agreed because of the American elections. It would
give the appearance of deserting our friends in an effort to placate those whom we thought to be less friendly. It is by no means clear that appeasement of this kind would be well directed. Finally, the Administration itself does not seem to share our qualms.

III.

The Washington Conversations and British Interests.

I have already said that the principle projects discussed at Washington were British projects, put forward by us and for our advantage. It may be convenient if I develop the argument here.

We can all agree that the greatest economic task which will face us internationally will be to restore our balance of international payments, which the war will have thrown seriously out of joint. We must certainly not accept any obligations inconsistent with our determination to provide Food, Work and Homes for 47 million people in these islands. But for this policy we shall need not only wise arrangements at home, but a steady volume of essential imports of food-stuffs and raw materials. Where are we to find the markets for the exports by which alone we shall be able to pay for these essential imports?

There is a characteristic of our trading position which has a vital bearing upon our future economic policy. It is this. The manufactured goods which we export are less essential to our customers than the food and raw materials which they export to us; and our exports to them have to be sold, to an increasing extent, in competition with their own manufactures. From this it follows that it is more important to us to be able to prevent our customers from imposing restrictions upon our exports than to have freedom to protect ourselves against imports from them. If we insist upon absolute freedom to limit imports other countries will take the same freedom to limit their imports. And because we cannot do without their exports while they can do without ours our bargaining position is likely to be a weak one. In the long run our customers would become increasingly self-sufficient while we remained dependent, and we could look forward only to ever diminishing standards of life.

Moreover, the plain, blunt and disagreeable truth must be faced that there is no mechanical device by which we can ensure that the rest of the world will maintain the population of these islands at a standard of life higher than that to which it is entitled by its economic activity. No amount of wishful thinking or of Hegelian dialectic will soften the harshness of this formidable truth. The solution of the problem with which we are faced must depend, therefore, upon the energy, the ingenuity and the technical skill and experience of the British people. One other thing we must do. We must ensure, as far as we can, that these qualities have full scope in the post-war world and that the advantages which we possess in the innate qualities of our people should not be lost through the imposition of trade barriers, import restrictions and the like against British exports.

There is also another characteristic of our trade position which it is necessary to bear in mind in considering the Washington Conversations. We do not sell in the same markets from which we buy. From the point of view of our future trade prospects, therefore, it is important that there is machinery for multilateral clearing, so that our purchases in one part of the world can be offset by our sales in another. The only alternative to something like the Stabilisation Fund or the Clearing Union is a system of currency blocs and bilateral trading arrangements through which purchases and sales would be balanced with each individual country or group.

There are political arguments, to which I will refer later and which seem to me to be decisive, against our adopting such a system of bilateral trading. But superficially it is attractive. It is easily understood. It is neat and tidy. It has a specious appearance of fair-mindedness and fair play; after all, why should we buy so much from the Argentine when the dirty Argentino buys so little from us? But it has very great disadvantages. It means that we force our export trade into a straight-jacket. Instead of producing those things for which they have a special aptitude, and in the production of which they have a competitive advantage, our manufacturers are forced to take up other lines for which they have less special aptitude and in which they have less competitive advantage.

Moreover, if we adopt the bilateral solution we cannot hope to reach any agreement limiting the protective barriers that other countries may erect against
our exports. As time goes on, our customers will throw off their dependence upon us which our bilateral bargains will have emphasised, and will adopt a protective policy for the excessive and uneconomic industrialisation of their countries. We may then see the sources of our essential supplies of raw materials and food stuffs drying up—sources which we can best hope to maintain by a reasonable policy outlawing immediate protectionism all round.

The multilateral solution will, of course, impose certain restrictions on our freedom of action. First, there would be limitations on the degree to which, and the methods by which, we could protect particular industries in this country. This limitation of our freedom involves real problems, and I will touch upon them at a later stage in this paper.

Secondly, we cannot hope to make substantial progress on these lines without a substantial modification of Imperial Preferences. The more extreme advocates of Imperial Preferences may regard this as little less than disastrous, but there is no doubt that they have their arguments too far. Thanks to Preferences, it is said "The Empire has in recent years taken half of our manufactured exports" (W.P. (43) 388). And again there is talk of "those Empire Preferences with the help of which practically half of our gross total exports have in recent years gone to the Empire . . . . it would be safe to say that the Empire trade was worth a great deal more to us than the trade of the rest of the world put together. How can we hope to retain the preferences upon which that trade is so largely based unless we give preferences in return?" (W.P. (43) 576).

In one sense, of course, it can be said that it is thanks to Imperial Preference that the Empire takes half of our manufactured exports, for before the Ottawa agreements the countries of the Empire absorbed not 50 but 45 per cent. of our export trade. In any other sense than this, however, the economic consequences of Imperial Preference must be admitted to be less satisfactory. For our exports to Empire markets fell from £324 million in 1929 to £235 million in 1938. It is true that our exports to countries outside of the Empire were contracted even more savagely (£405 million in 1929 as against £236 million in 1938). But the fact that our exports to the Empire did not fall quite so seriously as our exports to other countries can hardly be taken to prove that Preferences carry with them the solution of our balance of payments problem. A fall in the total value of our export trade from £729 million in 1929 to £471 million (a change from a favourable balance of payments of £258 million in 1929 to an unfavourable balance of £55 million in 1938) is to be explained by the very great increase in the barriers of every kind which were raised against them in the markets of the world. It was not only that the advantages of the Ottawa Agreements were offset by the high tariffs and import restrictions, some of them retaliatory in their nature, which were imposed against us in world markets. The very real advantage which we derived from the exchange deprecations in 1931 was partly lost when other countries, such as the United States, depreciated their exchanges against us in unnecessary retaliation.

From the point of view of the long-term prospects of our balance of payments the ideal arrangement would be one which permitted us to impose such restrictions as we thought necessary and denied the same right to other countries. It is obvious that such an ideal cannot be realised, but the policy which was agreed at Washington goes very near to it. It gives us, to quite a remarkable extent, the best of both worlds.

For it is of the essence of the Agreed Statements on Currency and Commercial Policy that a country with an unfavourable balance of payments is permitted to use expedients which are denied to a country with a favourable balance. In other words, we shall be allowed greater facilities if our balance of payments is unfavourable to depreciate sterling than are allowed to the United States, for example, while it has a favourable balance of payments, in the same way we shall be allowed a tight control of our imports, if our balance is unfavourable, while countries with a favourable balance are denied the use of the same expedients. Moreover, a country whose balance of payments is so favourable that its currency becomes "scarce" will have to face the prospect of discriminatory restrictions against its goods without the right to retaliate in kind.

It is important to consider whether the freedom of action which we enjoy under these proposals is sufficient for our purposes. A number of my colleagues are concerned, very properly, to ensure that we are not so tightly bound up with a world system that we are debarred from pursuing in the domestic field policies of expansionism and full employment, irrespective of what world conditions may be. It must be admitted that in 1931, at a moment of unparalleled
disequilibrium and depression, we were free to adopt a number of expedients—
tariffs, preferential arrangements with the Empire, quota restrictions and
currency depreciation—which enabled us to weather the storm as we could not
have done if our hands had not been free.

But the absolute freedom which we enjoyed before the war was largely
illusory, because every other country had precisely the same freedom and used
it in precisely the same way. Our exchange depreciation was offset by the
unnecessary American exchange depreciation; the inexcusable Hawley-Smoot
tariff of the Americans preceded our Ottawa agreements; and our tariff was
counterbalanced by a proliferation of trade barriers in our overseas markets.
Our freedom to manage our own affairs might have been more real in fact if it
had been more limited in theory and if we had been able, in return for some
sacrifice of our own liberty of action, to ensure that other countries did not abuse
theirs. If we adopt the policies which our delegation were discussing at
Washington we shall certainly lose some of our freedom to protect particular
industries and occupations in this country. But we shall gain immensely in our
freedom to import goods and to pay for them with exports. While we retain
considerable latitude in the management of our own exchange rates, we are
protected from a competitive siege of exchange depreciation, and we are assured
of some stability in exchanges and of a multilateral clearing system which will
greatly facilitate our export policy. And while we retain the right to impose
quantitative restrictions upon our imports when our balance of payments is
unfavourable, we ensure that countries with a favourable balance cannot impose
similar restrictions against our exports. At the same time we may well gain far
more than we lose from an all-round reduction in tariffs. Generally speaking, the
level of our own tariffs is lower than that of the tariffs over which Britain exports
have to climb in foreign markets. Our officials insisted at Washington that any
tariff proposal which we could accept must involve a more radical cut in high
than in low tariffs.

IV.
The Period of Transition.

Regarded as a long-term objective the policy of Article VII and the
Washington Conversations is clearly in our interests. It gives us as much liberty
of action as we can hope for in an imperfect world, and it protects us, in very
great measure, from the abuse by others of the freedom which they enjoy. But
it would be ridiculous to maintain that this policy will give us all that we want,
or all that we shall need, in the immediate post-war period. Special arrangements
will have to be made to cover the transitional period. And we may be well advised,
when we resume our discussions with the Americans, to concentrate more
thoroughly than we have so far done upon the economics of the transition. It is
certain that we shall require during this period a greater measure of freedom
(and assistance) than we shall be allowed under the long-term arrangements which
we are contemplating.

Some of my colleagues, I know, argue that we should concentrate exclusively
upon the transitional period and leave the long-term problem to take care of itself.
That, after all, is our policy at home. What reason is there for adopting a
different attitude in our external economic relationships? There are very good
reasons. In the first place we are going to need a measure of assistance from the
United States if we are to surmount our immediate post-war problems. We shall
have to get that assistance on terms which will not involve a repetition of the
difficulties of the debt situation after the last war. This is a problem which it
is going to be difficult for us to solve in any case. But a solution becomes
impossible if we start off with an alignment of policy which runs directly counter
to the American view of international economic relationships. We are entitled
to argue, if we like, that our view is as good as theirs and that it is only chicken-
livered pusillanimity to consider American susceptibilities to this extent. But we
cannot expect that such a line of argument will do very much to persuade the
Americans to meet us in our special difficulties.

That is not all. We have to consider the economic position of the world as
a whole. Our own position is not unique. We are not the only people who will
need a special latitude in the immediate post-war period. Others, besides
ourselves, will be faced with ardent problems of industrial demobilisation. Others
will be looking for full-employment policies. Others will be protecting their own
industries and seeking by subsidies, two-price systems and the like to expand
their exports. Unless, therefore, we take special measures to guard against it, the conditions of the transition will become normal and permanent. If we decide that a system of ordered multilateral trading will suit us best in the long run, we must see to it that the expedients which we and others are driven to adopt during the transition are directed towards this long-term goal and, as far as may be possible, made to conform to it. Dispensations there will have to be, but it is essential that they be granted by agreement among the Bishops and in accordance with the rules of the Church. Otherwise the sin will prove mortal.

Moreover, the transitional arrangements which other countries may adopt to restore their economies may accentuate, in some cases unnecessarily, the difficulties of our own transitional adjustments. Serious undervaluation of the currencies of our competitors or import restrictions, unnecessarily prolonged or unnecessarily severe, in our export markets, would increase our difficulties. While, therefore, we require special freedom of action in the transitional period, we are equally interested in achieving a moderate use of these freedoms and their termination at as early a date as is reasonable.

There is yet a further reason why we cannot apply to our external arrangements for post-war reconstruction the principle which we have chosen to apply to our internal reconstruction, namely, to concentrate on the transitional arrangements. We can make our own discussion of our domestic arrangements wait upon our own political convenience. But we cannot make the discussion of long-term economic arrangements by the Americans, the Russians, the Chinese, the French, the Dutch and the rest of the world wait upon our internal convenience. We must be prepared to discuss long-run external arrangements when others are prepared to discuss them; and if we miss the psychological opportunity offered to us now, it may never recur.

Our transitional arrangements should, therefore, be based upon the following considerations. We must lay great stress on their importance and must start to consider them in greater detail when we next meet the Americans. We must retain sufficient freedom of action to make sure that we can restore our position; we must ensure that the full obligations of the long-term settlement do not come into operation before we (and other countries) will be in a position to fulfil them; we must, however, take such steps as we can to ensure that the special freedoms of the transitional period are not abused and are not unnecessarily prolonged; and we must not allow these transitional difficulties to stand in the way of reaching agreement now on the longer-term arrangements. General suggestions of the way in which these principles might be applied to the transitional arrangements for monetary and commercial policy are outlined in more detail in the Annexes A and B.

I can see some force in the argument, which has been put forward with especial reference to Agriculture, that a transitional policy which is not avowedly permanent is no policy at all. Agriculture, it is agreed, is a long-term business and the farmer is not interested in the quick return. To give him, for example, an assured market in wheat up to a certain figure, in order to meet a particular crisis, and remove the assurance when the crisis has been met (partly as a result of his own efforts) is not practical politics. At any rate, it is not practical economics.

But we must not force this argument too far. We do not apply it to the emergency production of aircraft or munitions. We do not maintain that it is impracticable politically or economically to demand of the aircraft industry a vastly increased effort so long as our very being depends upon it, unless we are willing permanently to assure the industry of almost unlimited protection. Munitions production and food production are both essential to us in an emergency; and we may properly decide, even after the transition from the emergency is over, to give them special help and consideration. But in neither case is it essential to prolong emergency or transitional arrangements indefinitely without modification.

My colleagues will find in Annex B (paragraph 16) examples of the kind of latitude which will be allowed in the long run to the agricultural industry under the Washington proposals. Quantitative restrictions will not be permissible as a long-term measure, but moderate tariff protection and subsidisation* will be allowed. Guaranteed prices could still be offered to home

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* Whether or not any limit at all will be placed upon the subsidisation of agriculture is still a matter of Anglo-American dispute. A solution is tentatively proposed below (Annex B, paragraph 17 (iii)), which would retain for agriculture the ultimate right of unlimited subsidisation, but it is not yet possible to say how the Americans would receive this proposal if we did put it forward.
producers by subsidies, by levy-subsidy arrangements or by State import monopolies, provided that these arrangements were not used to raise the price of food to the home consumer excessively above the world price of imports. On the assumption that agriculture is to work its own passage to the fullest possible extent these provisions ought surely to give a sure foundation for a prosperous industry. It is only if agriculture is regarded as being permanently or whole-heartedly on the dole that they are inadequate. We are pledged to the farmer to support a prosperous agriculture, but that cannot be taken to mean that at whatever cost to the consumer in expensive food we are to maintain excessively uneconomic forms of agriculture at excessively inflated levels of production.

At Hot Springs we discussed principles of nutrition, the long-term application of which would stimulate in this country as elsewhere the demand for home-produced food-stuffs of a perishable but nutritive character, which we are well fitted to produce for ourselves. This may help to form the basis of a policy which is advantageous to our urban consumers, stimulating to our farmers and fully compatible with our desire to co-operate economically with other countries. This, combined with the freedoms which we retain under the Washington proposals, can, I submit, form a sure basis for a “healthy and well-balanced agriculture.”

There is an argument affecting the transitional period which appears in Annex A, paragraphs 35 to 38, and which, I think, it might be useful for me to comment on here. The critics of the currency scheme seem to believe that the existence of the long-term arrangements which were contemplated at Washington will jeopardise in some way our position during the transitional period. The Americans, so the argument runs, are putting up more than £300,000,000 for Relief. Under the currency scheme they are being invited to put up a further £750,000,000, and of this we are the beneficiaries to the extent of nearly half. It is a fact that, irrespective of the fate of the currency scheme, we shall require further and very substantial assistance from the Americans immediately the war is over. We cannot get along without it. Whatever may be the long-term advantages of the currency scheme, with all its indirect benefits, what we must have now is direct financial help. Are not the Americans likely to feel, if the commitment of the currency scheme is added to their commitment for U.N.R.R.A., that they have been generous enough? Are we not in danger, in our pursuit of the currency agreement, of losing the substantial advantages which, in one way or another, we must persuade the Americans to offer us?

Put in this way, the argument is a very formidable one. But if we put it more realistically, it is perhaps less impressive. We have great favours to ask of the Americans, favours which we must have and which, it may be, it will be most difficult for them to grant. We must do nothing, therefore, which will confuse the issue. We must do everything to create an atmosphere which will be favourable to us when we come to make our demands upon the Americans. How can this best be arranged? Clearly, there is only one way. We must reject out of hand proposals to which the Americans attach great importance, of which they are intensely proud, and in the formulation of which they have done a very great deal to meet our special difficulties. We must explain to them that we are no longer interested in the international arrangements which are under discussion between us. We are not looking for help for the United Nations. What we want is help for the United Kingdom. All of this having been made clear to the Americans, we shall have so endeared ourselves to them that incontinently they will meet all our demands.

V.

The Alternatives to Article VII.

I believe that the policy which we discussed at Washington will serve our interests better than any alternative. While I am far from sharing the gloomy apprehensions of some of my colleagues, I can give no assurance that we shall ever reach an agreement with the Americans on these lines. On a cool calculation of the probabilities, it must be regarded, I think, as unlikely. But this policy, if we can achieve it, is so much in our interests, and our first approach to the Americans has been so much more promising than we could have dared to hope, that it would be madness to draw back now. And the alternatives are so bad—and
in certain circumstances might be so desperately bad—that we would be unwise to embrace them until we are left without any other choice.

Perhaps, the most obvious alternative is that we should keep our hands free to make the best use of our bargaining strength as the main importing country of many important commodities. In 1938 the United Kingdom and Ireland accounted for 80 per cent, of total world imports of beef and mutton, 40 per cent, of world imports of wheat, 36 per cent, of zinc, and 19 per cent, of cotton imports. By a system of quantitative import regulation, of clearing agreements and discriminatory State purchases, we might be able to induce certain other countries to take our exports in return for the purchases which we make from them. The supplying countries could not readily submit to losing so important a market for their principal exports. At the same time we have, in the British Commonwealth and Empire and the Sterling Area, a number of prosperous and friendly countries with whom we could work together, in a system of mutual arrangements, to build over a wide area a progressively expanding economy. It can be argued, too, that all this would be healthy and in conformity with the spirit of the age which, it is said, is working all the time towards larger national groupings.

If we adopt a policy of this kind, we shall have, it is true, a fruitful example to guide us. This is not virgin land. A great deal of valuable pioneering has already been done for us by an eminent German financier. And he very nearly pull it off. Indeed, it can be argued very plausibly that Dr. Schacht was not misguided but only unfortunate. We shall have advantages that were denied to him. And Dr. Schacht was setting himself to create a war economy. We, by contrast, will be nourishing and fortifying the arts of peace.

It may well be that, in the end, we shall be thrown back upon attempting an alternative of this kind. If we fail to reach an agreement with the Americans on a multilateral policy, however, it is possible that we shall find some alternative less opposed to our interests than a policy of pure bilateralism. Before we chose the latter we had better consider very carefully what it is that we shall be doing and whither the road will lead us.

There is a vast difference between adopting this policy because the Americans have refused the other approach and embarking upon it before we have exhausted every other alternative. For the latter will be regarded by the Americans as a Declaration of War. I am convinced that this is so. It is not a matter of party alignment or of who wins the Presidential election. Short of our seeing the Secretary of State for India himself installed in the White House next January, with the Minister for Agriculture and Fisheries presiding, as Vice-President, over the Senate, it is impossible to conceive of any change in the political scene in the United States which will affect the truth of the proposition that the adoption by this country of a naked Schachtian policy will be taken as a Declaration of War. And indeed it will be nothing else for we shall be deliberately organising the world into rival economic groupings in which not private entrepreneurs but powerful Governments will be the protagonists. I cannot see what kind of a political structure we shall be able to erect on a foundation of this kind.

But the evil will not stop there. It is one thing to speak of the Commonwealth and Empire or the Sterling Area as the foundations and buttresses of our new economic policy. But what will be left of either when the gloves are off? What will be the position of Canada if we come to a break with the United States on so fundamental an issue? Canada is not a member of the Sterling Area. Her economic system is indissolubly bound up with that of the United States. I think that there can only be one answer to such a question. Sir Wilfred Laurier would walk again. Reciprocity would become a fact. And what of South Africa? Is it really conceivable that a country whose economy is based upon the production of gold would break with her best and perhaps her only customer? The position of Australia is more doubtful, although it is certain that the American market has many attractions for Australia. We may hope that the position of New Zealand would not be doubtful at all.

And then there is the Sterling Area. We are too apt to think of the Sterling Area as a kind of annex of the British Empire. It is nothing of the kind. It is a somewhat fragile association of countries who came together to pool their resources for certain limited purposes, and because they were willing to contribute what lay in their power to the conduct of a common war. But the arrangements which have been accepted during the war are most unlikely to survive it. For what advantages will we have to offer them against the inducements of the United States? It would not be politic—and indeed would it be necessary—to tell them the truth and to inform them that we were proposing to
make use of them to pull our chestnuts out of the fire for us. We cannot offer them gold or dollars. We cannot offer them the capital equipment of which they will be in need. This tenuous gossamer fabric of the Sterling Area would dissolve like a morning mist exposed to the direct rays of the noontday sun.

For these reasons I find some difficulty in understanding some of the arguments put forward in Annex A by the critics of the currency proposals which were discussed at Washington. It is said that the adoption of any scheme on these lines would make "the continuance of the sterling area impossible in any form in which we have known it hitherto." I have an uneasy feeling that the argument ought to be put the other way round and that for "impossible" we should read "possible"—if by "sterling area arrangements" we mean the old traditional practices. For, unless our position is strengthened by some expedient of the kind discussed at Washington, it is not easy to see how the long-standing banking practices of the sterling area can easily continue.

It is perfectly true that a system has been developed under war-time conditions by which "the various sterling countries turn over to us their surplus earnings of foreign exchange and we in return supply them with the foreign exchange they need, while transactions with the outside world are regulated by systems of exchange control, administered throughout the area on broadly similar lines." Very useful and convenient this system has been. And very convenient it would continue to be if we had a reasonable chance of our being able to maintain it. It is full of attractions for us. It is more difficult to see what charms it will have for the other members. For the maintenance of the war-time arrangements of the sterling area depends upon the transactions with the outside world of the area as a whole being restricted by systems of exchange control. In other words, Australia forgoes the luxury of American refrigerators or electric razors, New Zealand does without American automobiles, in order to pile up hard currencies in London and thus to further the common war effort. It has been a most striking example of the principle of the pooling of resources. It is possible that the system would not have worked so smoothly, even in these times, if it had not been for war-time restrictions upon shipping. It is certain that it would not work at all in normal conditions, and that the Dominions cannot be expected to submit to an indefinite lowering of their standards of living, not to win the war but simply to make London a peace-time financial centre. To invite them to do so is not going to preserve the sterling area. It is more likely to send it up in smoke.

Again, it is difficult to follow the line of reasoning which argues that "the inauguration of the scheme before the problem of the sterling balances has been satisfactorily resolved by direct negotiations between us and the holders of the balances, would make those negotiations more difficult because the discussion would start on the assumption that at the end of a limited Transitional Period sterling would be freely convertible." This can only mean that India, for example, foreseeing that the adoption of the currency scheme would greatly alleviate our difficulties, would be more exacting in her demands. This, however, is not an argument against the currency scheme in particular. If it is the case that an improvement in our position, in this or any other field, is only going to put us at the mercy of our creditors, then, clearly, we would do better to stay as we are. But I hope that it is not in this kind of a spirit that we are going to deal with India's sterling balances. I hope, rather, that it will be made clear to India that she, too, must make a financial contribution, in some form or another, to the war effort, and that the balances which she has acquired during the war are not to be regarded as the increment of ordinary commerce.

I have discussed some of the political consequences which would follow from a repudiation of Article VII. But there would also be economic consequences. The Americans would retaliate in kind. If it is our policy to make economic war upon the United States (and it is sheer humbug to pretend that this policy is anything else), then the United States will certainly make economic war upon us. So much has been made clear to us. And the armory of the United States is a very powerful one. By assisting the countries which would turn to their principal customers to establish their secondary industries the Americans would be able to expand their own exports at the expense of our markets. By subsidising secondary industries of their own, cotton-spinning, for example, they could lessen their dependence upon export markets for their stable crops, deny us the raw materials which we require for our own exports or, at any rate, raise the price against us, and at the same time create a new and formidable competition for us to meet in the markets of the world. All this, it may be said, would be grossly uneconomic. Of course it would. But we would surely be
unduly innocent if we were to suppose that we should be allowed an unchallenged monopoly in the new economics. Of course we should have to fight it out. And in this field, if anywhere, the longest purse—and it is not ours—would win.

These are some of the obstacles which we are likely to meet if we follow Dr. Schacht down the road of bilateralism. If, however, eventually we have to face them, our position will be stronger if we have exhausted, first of all, every alternative. If it has been made clear beyond all possible doubt that the Americans cannot be brought to any reasonable accommodation, if it is clear that we have been driven to other expedients not from choice but from necessity, then there is a chance, at least, that we shall be able to carry with us the members of the British Commonwealth and the Sterling Area. It is possible, too, that we shall be able to avoid a direct conflict with the United States if it can be shown that the choice is not ours. But to withdraw now from negotiations into which we have freely entered, to pursue a policy which we know is anathema to the Americans and which, even for us, is only a second best, would be to invite the sharpest conflict, and one in which we would find ourselves without allies.

VI.

Matters requiring Cabinet Decision.

It is necessary for the Cabinet now to decide whether or not to proceed with a policy generally on the lines discussed at Washington. We must make up our minds upon this main issue of principle. Only when this has been done will we be able to give the necessary guidance to the officials taking part in the conversations with the Dominions, which start on the 21st February.

We must make up our minds on the main issue. But if we decide that we are not going to reverse our policy and that we are going to proceed on the general line of the Washington Conversations, it is essential, in my view, that there should be no reservations of any kind. It has been suggested to me that a possible course might be to keep the Americans in play on Article VII in such a way as to ensure that the more difficult decisions would be indefinitely postponed and, perhaps, evaded altogether. But this would not only be dishonourable. It would be the most dangerous folly. I hope, therefore, that if the Cabinet decides to continue the line of policy which is outlined in this paper, it will be made clear to all concerned that the policy is to be carried through with conviction and a determination to make it successful.

Apart from the main issue, there are a number of subsidiary, but nevertheless important, matters on which Ministerial guidance will be required for the conduct of the talks with the Dominions. These questions are listed at the end of the Annexes to this paper.

It would be difficult to decide these complicated and somewhat technical issues at one, or even a series of Cabinet meetings. I would propose, therefore, that we decide now whether or not we wish to proceed on the general line of policy discussed at Washington; and, on the assumption that we agree to do so, a Committee of Ministers might be asked to decide before the 21st February on the line to be taken by our officials on the questions raised in Annexes A to F of this paper.

R. L.

Foreign Office, S.W. 1, 7th February, 1944.
ANNEX A.

(i) THE PROPOSAL FOR AN INTERNATIONAL MONETARY FUND.

I.

THE PRESENT STATE OF NEGOTIATIONS.

1. As a result of the autumn conversations in Washington and subsequent inter-bargaining, a draft text (subject to a few matters of secondary importance, about which correspondence is still taking place) has now been agreed with the United States Treasury on the expert level. This text is printed below under the title of a Statement of Principles.

2. It would not have been possible to achieve this agreed text if the United States Treasury had not given throughout the negotiations an exceedingly conciliatory spirit and a marked will to agreement. For, whilst the set-up of the scheme follows the American model more closely than the British, on matters of substance very large concessions have been made to our point of view.

3. The text does not bear a close resemblance to either of its predecessors. It was agreed at Washington to set aside both the British Clearing Union draft and the American Stabilisation Fund draft, and to start afresh with an agreed Statement of Principles, which would try to cover the major points on which Ministers and legislators would require to be satisfied, but would not attempt at this stage to incorporate the complete set of articles which will have to be drafted before the new institution can come into being. The result is much shorter than either of the original currency plans and occupies less than three pages of print.

4. It is suggested that the title of the new institution should be neither the International Clearing Union, as we originally proposed, nor the International Stabilisation Fund, as the Americans proposed, but the International Monetary Fund.

II.

THE MAIN OBJECTS OF THE PLAN.

6. The following is a statement of the main objects of the Plan and its attractions as seen more especially by our Washington representatives. Misgivings which are felt by some Treasury advisers are separately set out in the third section of this note.

7. It is a characteristic of British foreign trade that it often suits us to sell predominantly in certain countries and to buy predominantly in others. Our best sources of supply are not always our best markets. It will, therefore, help the expansion of our trade if we can re-establish the conditions generally prevailing before 1914, by which the proceeds of sales in one country could be freely applied to purchases in other countries. The Plan is calculated to secure this object after normal conditions have been reached, whilst requiring a full commitment to a multi-lateral clearing system in the transitional period, during which restrictions will be inevitable.

8. (i) By any suggestions made as a result of the debates in Parliament or by other Governments would then be considered by us in consultation with the United States Treasury. After that it would be for Ministers here to decide whether they were in a position to approve a Statement of Principles being passed on to a drafting committee as an instruction. If so, it has been agreed with the United States Administration that the Statement would constitute (as Mr. Morgenthau has asked) a definitive instruction which would not be departed from by either of our Governments without the agreement of the other.

[iii] Any suggestions made as a result of the debates in Parliament or by other Governments would then be considered by us in consultation with the United States Treasury. After that it would be for Ministers here to decide whether they were in a position to approve a Statement of Principles being passed on to a drafting committee as an instruction. If so, it has been agreed with the United States Administration that the Statement would constitute (as Mr. Morgenthau has asked) a definitive instruction which would not be departed from by either of our Governments without the agreement of the other.
10. (iv) Some part of the responsibility for maintaining equilibrium should be placed on the creditor countries, instead of throwing the whole burden, as hitherto, on the debtor countries. The placing of the Plan on a new foundation of great importance, not least because it has been put forward on the initiative of the American representatives without amendment from our side, and converted by the State Department and the Federal Reserve Board, as well as by the United States Treasury. Under the Clearing Union Plan the liability on a creditor country to maintain equilibrium by supporting the Fund, if it had failed to do so in some other way, was more clear and more definite. The American representatives felt that Congress would never accept an unlimited liability in advance, and that some other means must, therefore, be found for fixing responsibility on a chronic creditor country, which would be allowed to retain its earnings from the rest of the world and failed to return them to circulation either by consumption or by investment.

11. Put shortly in terms of the United States as an example, what the American representatives are offering the rest of the world is as follows. Up to an amount of £750 million they put at the disposal of the Fund the equivalent of any dollars which may accrue to them from a favourable balance of payments, as a result of their net foreign assets. Assuming what appears to be the cumulative balance thus built up is in danger of exceeding this total, they have the option of getting rid of their surplus on imports or overseas investment. Of course, if the Fund would not have the effect of making more American currency available, or of accepting the conditions which become applicable when the Fund has declared dollars to be a "scarce" currency, then this third alternative means in effect that American exporters can no longer claim payment for their goods in excess of the amount which the United States is making available on the other side of the account by imports or by lending. All the other countries of the world become entitled forthwith to put any form of restrictions they choose in the way of accepting American goods and in the way of paying for any they do accept. To put this third alternative into effect would, it is true, cause great trouble and technical difficulty all round. It was, however, the view of the American representatives that from their point of view the third alternative would be so intolerable that it could never be allowed to come into practice and that their country would be forced to adopt one of the other alternatives. That, indeed, is what they wanted to see forced upon them. They also gave as an additional reason why this would be the outcome, that, if American exporters were to be required to accept devalued dollars, they will most probably accompany slump conditions in the United States. In such circumstances the American Administration could never afford to see the whole of its export industries thrown into confusion. The American representatives were fully aware of the implications of their own proposal. They were moved by their consciousness of how serious to the world any failure to solve the problem would be, and of the importance, therefore, of taking every possible step to ensure a solution. Nevertheless, the offer is a signal mark of their courage, of their fair-mindedness and of their sense of responsibility to the other nations of the world.

12. This proposal represents, therefore, a revolutionary change for the better compared with the position in the inter-war period. The American representatives offer voluntarily on behalf of their country to abate its former strangulation on the world's economy and to offer safeguards against its hazards. This proposal forces deflation on others. Moreover, this particular provision has been published and Congress is aware of it; yet, so far, it has not been the target of a mass insurrection. We are, therefore, on our part to reject so fair an offer and to reinspect the return to the chaos and irresponsibility of the former lack of system.

13. (v) Ministers will be particularly concerned with the adequacy of the provisions to secure elasticity of exchange rates. In this respect the American representatives have never departed widely from their original proposals, which seemed to aim at extreme rigidity of exchange on the model of the former gold standard—or, at any rate, could be so represented. The Washington Delegation was aware that such arrangements could not be accepted by the British Cabinet and would be inevitably rejected by Parliament. As the result of prolonged discussions, the procedure as set forth in Clause 5 of the Statement of Principles below emerged; it may be summarised as follows:

(a) The principle of change both in the value of individual currencies and in the value of gold itself, to suit changing circumstances, is expressly recognised.

(b) A proposal for change by a member country has to be considered judicially by the Fund, from the point of view whether it is in fact required to remedy disequilibrium; and, if in the actual circumstances it is required, the Fund may not refuse it on the ground of the explanation of disequilibrium should be sought rather in the domestic, social or political policies of the applicant member, in which case it must be that country's responsibility to effect it.

(c) Changes not exceeding 10 per cent. in the aggregate may be made by a member country acting, after consultation, but unilaterally.

(d) Changes of a further 10 per cent. may be made unilaterally, unless the Fund has refused approval within two days of the application for a change having been made.

(e) If a country is dissatisfied with the Fund's decision on this matter, it can terminate its membership of the Fund and resume its full freedom of action forthwith, without notice and without penalty.

(f) The Fund is particularly required to take into consideration the extreme uncertainties likely to prevail when the initial partialies are fixed, and, during the transitional period, to allow a member asking for a change the benefit of any reasonable doubt.

14. These proposals seem to combine satisfactorily an orderliness with a sufficient ultimate freedom of action to individual members. They certainly cannot be represented as being aimed at gold-standard rigidity. Their whole purpose is to provide a proper means to secure orderly changes in exchange rates and to suit changing circumstances in the value of individual currencies and in the value of gold itself, to suit changing circumstances, is expressly recognised.

15. Particular attention is invited to (c) above. The American representatives were at first most reluctant to accept this provision, but were in the end persuaded to depart widely from their original proposals, which seemed to aim at extreme rigidity of exchange on the model of the former gold standard—or, at any rate, could be so represented. The Washington Delegation was aware that such arrangements could not be accepted by the British Cabinet and would be inevitably rejected by Parliament. As the result of prolonged discussions, the procedure as set forth in Clause 5 of the Statement of Principles below emerged; it may be summarised as follows:

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(f) The Fund is particularly required to take into consideration the extreme uncertainties likely to prevail when the initial partialies are fixed, and, during the transitional period, to allow a member asking for a change the benefit of any reasonable doubt.
purposes of the institution are in risk of infringement, thus keeping them as an instrument, entirely passive in all normal circumstances, the right of initiating being reserved to the Central Banks of the member countries. The American representatives had set out in their Speeches the wish to see the new institution carry out the functions of the new institution. In their eyes, it should have wide discretionary and policing powers and should exercise something of the same measure of authority in the member countries as the existing Central Banks. In Banks in turn are accustomed to exercise over the other countries. 

require special legislation which could be represented involving a new international unit which the initial difference of approach by the Clearing Union proposals but was only mentioned in substance and legal effect. A given set of proposals can be drafted in terms of either set-up so as to be identical in matter of technical form. A given set of proposals can be drafted in terms of either set-up so as to be identical in technical form. A given set of proposals can be drafted in terms of either set-up so as to be identical in technical form.

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appreciating, face to face, the great efforts made on the distance of giving the member countries as much certainty and by the Stabilisation Fund respectively, is as follows. Under the Clearing Union proposals the member countries were to bank with the institution, where they would have accounts on which they were free to operate in terms of a new international unit of account, national currencies being replaced by a new international currency.

have been in the end settled on the expert level. In the final draft, therefore, all the technical matters at issue, except one, have been in the end settled on the expert level.

The one matter outstanding which flows from an initial difference of approach by the Clearing Union and by the Stabilisation Fund respectively, is as follows. Under the Clearing Union proposals the member countries were to bank with the institution, where they would have accounts on which they were free to operate in terms of a new international unit of account, national currencies being replaced by a new international currency.

should have wide discretionary and policing powers and should exercise something of the same measure of authority in the member countries as the existing Central Banks. In Banks in turn are accustomed to exercise over the other countries. 

be increased by the high-lighting in the proposal of a new international currency.
26. While accepting the main objectives, they fear that the scheme contains immediate disadvantages and serious dangers. For example, the continuance of the sterling area as we have known it hitherto would be seriously prejudiced and the difficulties of handling the problem of our sterling balances would be increased. The Exchange Clause may be quite reasonable for limiting a deliberate devaluation of the currency of any country, but most devaluations in the past have been involuntary and the possibility that they may again be involuntary does not seem to be covered. The clause about the transitional period causing anxiety in case it should prove dangerous in practice. No country without strong monetary reserves would be able to maintain definite parities of exchange and to support them by the use of its money reserves. This might force us to buy from some sources of supply rather than others, and if this went on for a long period, as is quite likely, we should expose ourselves to a charge of discrimination in trade and faith.

27. The Scheme is admittedly designed for the long term when international equilibrium has been reasonably established. There is no dispute that agreement on long-term objectives would be helpful for the implementation of the Plan, however, goes far beyond a statement of objectives; it is a detailed scheme containing the rules which will be binding upon the signatory countries and the Executive Management. It is possible that when the scheme is published this agreement on long-term objectives would be helpful for the implementation of the Plan. If we were to commit ourselves to it we should expose ourselves to a charge of discrimination in trade and faith.

28. On this view it is open to serious question whether we can see far enough ahead for ourselves and others closely associated with us to take the responsibility of attempting to secure a binding international agreement on long-term objectives. We considered the possibility of a multilateral clearing plan. If we were to commit ourselves to it we should have to join in exerting pressure upon the Dominions and India and the European Allies to overcome objections and misgivings which on merits we may largely share.

29. The chief criticisms which underlie these misgivings may be thus briefly stated.

(a) Multilateral Clearing.

30. We could not hope to discharge for an indefinite period the obligation which constitutes the central purpose of the Scheme, namely, to make sterling freely convertible. This is not only because of the problem of sterilizing balances which we cannot expect to block but would last longer than the transitional period when we have to approach the Americans for additional direct gold. In any one year we may only draw 25 per cent. of our quota, i.e., £80 million. This will be inadequate to draw us through our adverse balance on current account.

31. It may well be thought unsatisfactory that the shape of a Scheme to help international trade should begin by recognizing the inevitable contracting out from the major purpose of the Scheme by the country which, before the war, had the largest international trade.

(b) Exchange rates.

32. We, and other countries, would be required from the outset to maintain definite parities of exchange and to support them by the use of our monetary reserves. These parities could be varied from time to time with the approval of the Fund, but at any time there would be definite parities in terms of gold which we would have to support.

33. At present we have a managed exchange rate: it is not formally tied to gold or to any other currency. We are free to appreciate or depreciate sterling and free to let it find its own level with no fixed parity without any obligations except those of the Tripartite Agreement for consulting the United States and France.

84. Although the major international exchange rates should not be changed suddenly without consultation between the parties chiefly concerned, the technique of agreement on long-term objectives would make it impossible to remove all " pegs " and allow the rate to move to whatever level proves appropriate. There is a wide difference between this and a formal international obligation to maintain a definite parity. It is often impossible to determine in advance the level at which it would be wise to try to check a further fall by the free use of limited monetary reserves. In 1931 sterling fell by nearly one-third before a process of market recovery began; and any attempt to hold it up before this point was reached might have proved futile.

(c) Inadequacy of credit.

35. The credit facilities provided by the Scheme are not distributed according to the immediate needs of the countries which have suffered the greatest economic damage from the war. They are an inadequate for our own discernible needs that we must protect ourselves against being compelled to use them up for fear that we prejudice our chances of obtaining additional direct gold. They cannot be used by the Fund for its purpose of the Plan. This is a large sum which Congress and American public opinion might expect together with their contribution towards U.N.R.R.A., as a fair discharge of their moral obligation to put the world economically on its feet, and if we contemplate having to approach the Americans for additional direct gold, we might well be disappointed.

36. In this situation we are contemplating suggesting a clause to the Americans which would make it plain that a country is not expected to use the financial facilities of the Fund so long as it exercises its contractual rights on multilateral clearing; this is to leave us free to make the best bargain we can with the Americans.

37. The United States would be committed formally and forthwith to put up £750 million for the purpose of the Plan. This is a large sum which Congress and American public opinion might expect together with their contribution towards U.N.R.R.A., as a fair discharge of their moral obligation to put the world economically on its feet, and if we contemplate having to approach the Americans for additional direct gold, we might well be disappointed.

38. In this situation we are contemplating suggesting a clause to the Americans which would make it plain that a country is not expected to use the financial facilities of the Fund so long as it exercises its contractual rights on multilateral clearing; this is to leave us free to make the best bargain we can with the Americans.

39. In paragraph 7 (e) of W.P. (43) 888 we had a clause which was important of our " passivity," that, in order that sterling should not be prejudiced by the operation of an international monetary authority, the Fund should be entirely passive and should not be in a position in any way to deal in any currency. In order to safeguard this position it was proposed (1) that the subscriptions of member countries to the Fund should not include any contributions in their currencies but should be composed entirely of gold and non-negotiable Government securities; (2) that the subscription so composed should be kept as a security for the liabilities of the countries concerned and should not be used by the Fund for its ordinary operations; and (3) that the transactions of the Fund should be conducted in terms of an international " money of account," which would effectively distinguish them from any dealing in exchanges. From our discussions with the European Allies it was believed that they would support us unanimously in pressing for these fundamental conditions.

40. None of these conditions is fulfilled.

41. In place of the composite but related safeguards suggested to ensure " passivity," the scheme has not only one safeguard, namely, that the Fund cannot deal in any currency. The section of the Act which provided for the provisional use of the currency on the request of a member bank in exchange for that member bank's own currency of gold.

42. It is feared that this safeguard is more effective on paper than it would be likely to prove in practice. It is possible that when the scheme is published this...
provocative will be widely regarded as anomalous. Why put the Fund in possession of national currencies if they are not permitted to use them at their discretion to help to keep exchange rates reasonably stable, to watch over the position in each country and to offer them a stabilizing influence.

43. Because the scheme, despite the very important modifications secured by our Delegation, still has the essential shape of an Exchange Equalization Fund, each member country would use "initiative," however discreetly. If they found that they were beginning to accumulate large holdings of a particular currency, nearing the limit of the permissible holdings, banking traditions would dispose them to try to make their position more liquid by suggesting to some member country that they should temporarily exchange part of the surplus currency for their own currency. Such an initiative, however discreet, would, so it is said, become known and the "surplus" currency would be regarded as open to some suspicion. Since sterling is bound to be a "surplus" currency for some years after the war, this is a possibility that we are bound to consider.

(c) The Sterling Area

44. The scheme must tend to weaken the cohesion of the sterling area, and would probably make its continuance impossible in any form in which we have known it hitherto. The sterling area has evolved naturally from the close economic relations which exist between the British Commonwealth, which includes the most important part of the British Empire, and several other countries. Before the war the arrangements were purely informal; the countries belonging to the area kept their monetary reserves in London in the form of sterling balances; they bought London gold and provided London with their surplus gold; and their currencies were for the most part tied to sterling rather than to gold. Thus within the sterling area there was exchange stability and multilateral clearing. During the war these practices have been developed into more formal arrangements under which the various sterling countries turn over to us their surplus earnings of foreign exchange, and we in return supply them with the foreign exchange they need, while they buy sterling balances and foreign exchange from us, and thus exchange control, administered throughout the area on broadly similar lines. These arrangements, though they could not, of course, be continued in peace time in their present form, have been of the greatest advantage to us during the war. Under the monetary scheme, the Dominions and India would be independent member countries with their own individual quotas, and their own separate obligations to make their currencies freely convertible, to provide for exchange control, and to maintain the various parities of their currencies subject to the various provisos which the scheme contains. It is evident that one part of the area might feel able to dispense with some of the transitional safeguards before others could do so; and for this and similar reasons, it seems inevitable that the area would disintegrate as a result of the operation of the scheme.

45. Under the monetary scheme, the Dominions and India would be independent member countries with their own individual quotas, and their own separate obligations to make their currencies freely convertible, to provide for exchange control, and to maintain the various parities of their currencies subject to the various provisos which the scheme contains. It is evident that one part of the area might feel able to dispense with some of the transitional safeguards before others could do so; and for this and similar reasons, it seems inevitable that the area would disintegrate as a result of the operation of the scheme.

46. When the two original schemes were published, uninstructed vocal opinion in America fixed on the American share in the question of voting rights and control. As so much American money will be involved in this scheme, it is inevitable that the same questions would arise again. The American Treasury have generously accepted voting arrangements on the Board of Directors which would not give the American managers a majority position. It is not certain that such a suggestion would commend itself to American opinion in its present mood. Moreover, it is not the voting right of the directors that really matters on the daily business of the Fund, but the competence and impartiality of the executive managers. In the present atmosphere of politics in the United States, it seems highly unlikely that such a management would be chosen without very full regard for purely political considerations.

47. The sterling area in the form in which it has been evolved during the war will no doubt have to be modified for post-war conditions. On the other hand, it is quite likely that some other important areas, including the French, Belgian and Dutch Empires, whose economy is in some respects comparable to our own, might wish to associate themselves with the sterling area for certain purposes. Progressively over that expanded area multilateral clearing could be introduced and the major currencies in the area could establish links with the United States which might make it practicable to carry multilateral clearing much further and faster than would be possible under the currency scheme.

48. One aspect of the sterling area system in the war creates very important liabilities for us, viz., the sterling balances held by one or two members, particularly India and Egypt.

49. The inauguration of the scheme before the problem of the sterling area has been satisfactorily resolved by direct negotiation between us and the holders of the balances would make those negotiations more difficult because the discussions would start on the assumption that at the end of a limited period sterling balances would be freely convertible. The fact that we would be able to appeal to a clause in the scheme which, in substance, distinguishes abnormal war balances from future balances on current account would not make the clause more palatable or its uniqueness free from suspicion.

(f) Relations with Commercial Policy

50. The Currency Scheme is at a stage far in advance of Commercial Policy, although public opinion would expect the two Schemes to march forward together. The close relation of the policies is important to us because some of the safeguards open to us if we get into difficulties and would depend upon the shape of agreed Commercial Policy.

51. Informed opinion would want to be satisfied that the United States was likely to pursue a commercial policy likely to facilitate balanced payments with the outside world. On the other hand, our ability to defend any parity for sterling against adverse pressure might be seriously affected by undertakings, e.g., as regards import restrictions, which we might later be expected to give.

(g) "Scarce currencies"

52. Great importance is attached to Clause 7 of the Agreement on Scarce Currencies, for the reasons explained in the preceding sections of this note (paragraphs 10-12). The clause is declaratory and it may be that the acceptance of it by the American Administration as a whole would be sufficient to prevent the United States consciously allowing the dollar to become scarce because they are prepared to buy and will not invest the dollar to become scarce because they are prepared to buy and will not invest the dollar to become scarce because they are prepared to buy and will not invest...
for the problems of reconstruction, it will not be
regarded as an international necessity, even with possible
deficiencies, in the same way as U.N.R.R.A.
was.
55. But for such a novel and detailed international
monetary plan a wide acceptance is almost necessary from
the beginning. It is by no means clear that it
will be acceptable in this sense to the opinion of the
Americans, either Congress or among the informed
public. As far as we can judge, it will be regarded with
hesitancy by the New York banking house, whose
co-operation in it will be essential if it is to endure.
56. In these circumstances, and particularly because
of the present uncertainties on a solution of the
transitional and of the relation between
disequilibrium in the international balance of payments
problems. The resources of the Fund would be
available under adequate safeguards to help member
countries to correct maladjustments in their balance
of payments without resorting to measures destructive
of employment. The Fund is expected to provide the
bute in this way to the maintenance of a high level
of international monetary co-operation. The Fund is intended to facilitate the
permanent institution for international monetary
balanced growth of international trade and to contri­
buting in this way to the maintenance of a high level of
employment. The Fund is designed as a
permanent institution for international monetary
co-operation. The Fund is intended to facilitate the
balancing of international trade and to contribute
in this way to the maintenance of a high level of
employment. The Fund is expected to provide the
mechanism for consultation on international monetary
problems. The Fund is intended to provide the
infrastructure of international cooperation to help member
countries to maintain exchange stability during the transitional period;
giving them time to correct maladjustments in their balance
of payments without resorting to measures destructive
to national or international prosperity.

2. Purpose of the Fund.
(i) To promote exchange stability to maintain
orderly exchange arrangements among member
countries and to avoid competitive exchange
depreciation.
(ii) To assure multilateral payments facilities on
current transactions among member countries and to help eliminate foreign exchange restrictions that
hamper the growth of world trade.
(iii) To shorten the period and lessen the degree of
disequilibrium in the international balance of payments
of member countries.
(iv) To give confidence to member countries by the
provision of actual and potential support in the
attainment of these purposes.

3. Subscription to the Fund.
(i) Member countries shall subscribe in gold and in
their local funds amounts (quotas) determined by
a formula to be agreed, which will amount altogether to
about $8 billion if all the United Nations and the
countries associated with them subscribe to the Fund
(corresponding to about $10 billion for the world as
a whole).

(ii) The obligatory gold subscription of a member
country shall be fixed at 25 per cent. of its subscription
(quotas) or 10 per cent. of its holdings of gold
and gold-convertible exchange, whichever is the
smaller. The amount of the holdings of gold and
gold-convertible currency for the purposes of this
clause and clause 4 (vii) below shall be determined
by agreement between each member country and the
Fund.

4. Transactions with the Fund.
(i) Member countries shall deal with the Fund only
through their Treasury, Central Bank, Stabilisation
Fund, or other fiscal agencies. The Fund's account
in a member country shall be kept at the Central
Bank of the member country.
(ii) A member shall be entitled to buy another
member's currency from the Fund in exchange for its
own currency on the following conditions:
(a) the member represents that the currency
demanded is presently needed for making payments
in that currency which are consistent
with the purposes of the Fund;
(b) the Fund has not given notice that its holdings
of the currency demanded have become
crude, in which case the provisions of 7 below shall be determined
by agreement between each member country and the
Fund.
(c) the Fund's total holdings of the currency offered
have not increased by more than 25 per cent
of the member's quota during the previous
twelve months, and do not exceed 200 per
cent. of the quota.
(d) the Fund has not previously given appropriate
notice that the member is suspended from
making further use of the Fund's resources on
the ground that it is making use of them in a
manner contrary to the purposes and policy
of the Fund; and
(e) the Fund may, in its discretion and on conditions
which safeguard its interests waive any of the
conditions above.

(iii) Subject to (iv) below, operations on the Fund's
account will be limited to transactions for the purpose
of supporting a member country, on the member's
initiative and subject to the provisions of (ii) above,
with another member's currency in exchange for its
own currency or for gold.

57. The questions for settlement by the Cabinet are:

(i) whether the Plan is provisionally approved;
(ii) if so, what the line of procedure as regards
Mr. Morgenthau should stand, namely,
that upon publication being agreed upon
between the two Governments the Statement
of Principles should be communicated to the
other Governments concerned and then to be
the subject of debates in Parliament here,
Ministers explaining that at this stage and prior to the expression of views in Parlia­
ment, Ministers have no way committed to the
Statement beyond believing that it embodied
a Plan which deserved the most serious
consideration (paragraph 8);
(iii) whether a communication should be made to
Washington at the first convenient oppor­
tunity leading up to representations in the
sense of paragraphs 22 and 23 in regard to the
transitional period;
(iv) the broad lines to be followed in the forthcoming discussions with the Dominions.

(ii) STATEMENT
OF PRINCIPLES.

JOINT STATEMENT BY EXPERTS OF UNITED AND
ASSOCIATED NATIONS ON THE ESTABLISHMENT OF AN
INTERNATIONAL MONETARY FUND.

Sufficient discussion of the problems of international
monetary co-operation has taken place at the technical
level to justify a statement of principles. The experts
of the United and Associated Nations who have
participated in these discussions are of the opinion
that the most practicable method of ensuring inter­
national monetary co-operation is through the estab­
ishment of an International Monetary Fund. They
have set forth below the principles which they believe
should be the basis for this Fund. Governments are
not asked to give final approval to these principles
until they have been able to gather the views of
Parliament, of the Dominions, of the United States and
of the European Allies and other United Nations.

Preamble.


The International Monetary Fund is designed as a
permanent institution for international monetary
co-operation. The Fund is intended to facilitate the
balancing of international trade and to contribute
in this way to the maintenance of a high level of
employment. The Fund is expected to provide the
mechanism for consultation on international monetary
problems. The Fund is intended to provide the
infrastructure of international cooperation to help member
countries to maintain exchange stability during the transitional period;
giving them time to correct maladjustments in their balance
of payments without resorting to measures destructive
to national or international prosperity.

2. Purpose of the Fund.

(i) To promote exchange stability to maintain
orderly exchange arrangements among member
countries and to avoid competitive exchange
depreciation.
(ii) To assure multilateral payments facilities on
current transactions among member countries and to help eliminate foreign exchange restrictions that
hamper the growth of world trade.
(iii) To shorten the period and lessen the degree of
disequilibrium in the international balance of payments
of member countries.
(iv) To give confidence to member countries by the
provision of actual and potential support in the
attainment of these purposes.

3. Subscription to the Fund.

(i) Member countries shall subscribe in gold and in
their local funds amounts (quotas) determined by
The Fund will be entitled at its option, with a view to preventing a particular member's currency from becoming "scarce":—

(a) to borrow its currency from a member country;
(b) to offer gold to a member country in exchange for its currency.

(c) So long as a member country is entitled to buy another member's currency from the Fund in exchange for its own currency, it shall be prepared to buy its own currency from any member country with that member's currency or with gold. This shall not apply to currency for gold is expected, provided it can do so with equal advantage, to acquire the currency by the sale of gold to the Fund. This shall not preclude the sale of newly mined gold by a gold-producing country at any market price.

(d) A member country may repurchase from the Fund for gold any part of the latter's holdings of its currency.

(e) A member country, as long as its holdings of gold and gold-convertible exchange have increased, is entitled to repurchase from the Fund all or part of the latter's holdings of its currency. When a currency is thus declared scarce, the Fund shall inform member countries and propose an equitable method of apportioning the scarce currency. When a currency is thus declared scarce, the Fund shall issue a report embodying the causes of the scarcity and containing recommendations designed to bring it to an end.


(i) When it becomes evident to the Fund that the demand for a member country's currency may soon exhaust the Fund's holdings of that currency, the Fund shall consult each member country and propose an equitable method of apportioning the scarce currency. When a currency is thus declared scarce, the Fund shall issue a report embodying the causes of the scarcity and containing recommendations designed to bring it to an end.

(ii) A decision by the Fund to apportion a scarce currency shall operate as an authorization to a member country, after consultation with the Fund, temporarily to restrict the freedom of exchange operations in the affected currency, and in determining the manner of restricting the demand and rationing the limited supply among its nationals the member country shall have complete jurisdiction.

8. Management.

(i) The Fund shall be managed by a Board of Directors and Executive Committee representing the members.

(ii) The distribution of basic voting power shall be closely related to quotas, but no member shall be entitled to cast more than one-fifth of the aggregate votes.

(iii) All matters shall be settled by majority, except that a change in the basis of determining quotas shall require a four-fifths vote, and no member's quota may be changed without its consent.


(i) A member country may withdraw from the Fund by giving notice in writing.

(ii) The reciprocal obligations of the Fund and the country are to be liquidated within a reasonable time.

(iii) After a member country has given notice of its withdrawal from the Fund, the Fund may not dispose of its holdings of the country's currency except in accordance with the arrangements made under (ii) above. After a country has given notice of withdrawal, its right to utilize the resources of the Fund is subject to the approval of the Fund.

10. Obligations of Member Countries.

(i) Not to buy gold at a price above the parity of its currency, nor to sell gold at a price below the parity of its currency.

(ii) Not to allow exchange transactions in its currencies of other members at rates outside a prescribed range based on the agreed parities.

(iii) Not to impose restrictions on payments for current international transactions with other member countries.
for the problems of reconstruction, it will not be regarded as an international necessity, even with possible deficiencies, in the same way as U.N.R.R.A. was regarded.

55. But for such a novel and detailed international monetary plan a wide acceptance in almost necessary from the beginning. It is by no means clear that it will be acceptable in this sense to the opinion of the Americans, either Congress or among the informed public. As far as we can judge, it will be regarded with hostility by the prevailing banking system, whose co-operation in it will be essential if it is to endure.

56. In these circumstances, and particularly because of the present uncertainties on a solution of the transitional period, and of the relation between decisions on commercial policy and the Currency Scheme, those at the Treasury who hold the views described above would urge that early publication of the Scheme is desirable, but that Ministers should no more than present it for the careful attention of Parliament, without committing themselves to recommending its early inauguration in its present form, until they have been able to gather the views of Parliament, of the Dominions, of the United States and of the European Allies and other United Nations.

(ii) STATEMENT OF PRINCIPLES.

JOINT STATEMENT BY EXPERTS OF UNITED AND ASSOCIATED NATIONS ON THE ESTABLISHMENT OF AN INTERNATIONAL MONETARY FUND.

Sufficient discussion of the problems of international monetary cooperation has taken place at the technical level to justify a statement of principles. The experts of the United and Associated Nations who have participated in these discussions are of the opinion that the most practical method of assuring international monetary co-operation is through the establishment of an International Monetary Fund. They have set forth below the principles which they believe should be the basis for this Fund. Governments are not asked to give final approval to these principles until they have been embodied in the form of definitive proposals by the delegates of the United and Associated Nations meeting in a formal conference.

1. Preamble.

The International Monetary Fund is designed as a permanent institution for international monetary co-operation. The Fund is intended to facilitate the balanced growth of international trade and to contribute in this way to the maintenance of a high level of employment. The Fund is expected to provide the machinery for consultation on international monetary problems, and co-operation through their Treasury, Central Bank, Stabilisation Bank of the member country.

2. Purposes of the Fund.

(i) To promote exchange stability, to maintain orderly exchange arrangements among member countries, and to avoid competitive exchange depreciation.

(ii) To assure multilateral payments facilities on current transactions among member countries and to help eliminate foreign exchange restrictions that hamper the growth of world trade.

(iii) To shorten the period and lessen the degree of disequilibrium in the international balance of payments of member countries.

(iv) To give confidence to member countries by the provision of actual and potential support in the attainment of these purposes.

3. Subscription to the Fund.

(i) Member countries shall subscribe in gold and in their local funds amounts (quotas) determined by a formula to be agreed, which will amount altogether to about $8 billion if all the United Nations and the countries associated with them subscribe to the Fund (corresponding to about $10 billion for the world as a whole).

(ii) The obligatory gold subscription of a member country shall be fixed at 25 per cent. of its subscription (quota) or 10 per cent. of its holdings of gold and gold-convertible currency, whichever is the smaller. The amount of the holdings of gold and gold-convertible currency for the purposes of this clause and clause 4(vii) below shall be determined by agreement between each member country and the Fund.

4. Transactions with the Fund.

(i) Member countries shall deal with the Fund only through their Treasury, Central Bank, Stabilisation Fund, or other fiscal agencies. The Fund's account in a member's currency shall be kept at the Central Bank of the member country.

(ii) A member shall be entitled to buy another member's currency from the Fund in exchange for its own currency, provided that—

(a) the member represents that the currency demanded is presently needed for making payments in that currency which are consistent with the purposes of the Fund;

(b) the Fund has not given notice that its holdings of the currency demanded have become scarce, in which case the provisions of 7 below come into force;

(c) the Fund's total holdings of the currency offered have not increased by more than 25 per cent. of the member's quota during the previous twelve months, and do not exceed 200 per cent. of the quota;

(d) the Fund has not previously given appropriate notice that the member is suspended from making further use of the Fund's resources on the ground that it is making use of them in a manner contrary to the purposes and policy of the Fund; and

(e) the Fund may in its discretion and on conditions which safeguard its interests waive any of the conditions above.

(iii) Subject to (iv) below, operations on the Fund's account will be limited to transactions for the purpose of supplying a member country, on the member's initiative and subject to the provisions of (ii) above, with another member's currency in exchange for its own currency or for gold.
The Fund will be entitled at its option, with a view to preventing a particular member's currency from becoming "scarce"—

(i) to borrow its currency from a member country;
(ii) to offer gold to a member country in exchange for its currency.

So long as a member country is entitled to buy another member's currency from the Fund in exchange for its own currency, it shall be prepared to buy its own currency from that member at the Fund's currency or with gold. This shall not apply to currency subject to restrictions in conformity with 10 (iii) below or to holdings of currency which have accumulated as a result of transactions of a current account nature effected before the member country's restrictions on multilateral clearing maintained or imposed under 11 (ii) below.

A member country desiring to obtain, directly or indirectly, the currency of another member country for gold is expected, provided it can do so with equal advantage, to acquire the currency by the sale of gold to the Fund. This shall not preclude the sale of newly mined gold by a gold-producing country on any market.

The Fund for gold any part of the latter's holdings of its currency, except in accordance with the arrangements for current transactions or to delay unduly the transfer of funds in settlement of commitments.

5. Par Values of Member Currencies.

The par value of a member's currency shall be agreed with the Fund when it is admitted to membership, and shall be expressed in terms of gold. All transactions between the Fund and members shall be at par, subject to a fixed charge payable by the member making application to the Fund, and all transactions in member currencies shall be at rates within an agreed percentage of parity.

If a change is required, necessary to restore equilibrium, because of the domestic social or political policies of the country applying for a change in the par value of its currency, the Fund shall not reject a requested change, subject to the approval of the Fund, and no member shall be entitled to cast more than one-fifth of the aggregate votes.

The Fund shall approve a requested change in the par value of a member's currency, if it is essential to the correction of a fundamental disequilibrium. Changes shall be made only with the approval of the Fund, subject to the provisions below.

The Fund shall issue a report embodying the causes of the scarcity and containing recommendations designed to bring it to an end.

(i) Not to impose restrictions on payments for current transactions or to delay unduly the transfer of funds in settlement of commitments.

7. Apportionment of Scarce Currencies.

If it becomes evident to the Fund that the demand for a member country's currency may soon exhaust the Fund's holdings of that currency, the Fund shall so inform member countries and propose an equitable method of apportioning the scarce currency. When a currency is thus declared scarce, the Fund shall issue a report embodying the causes of the scarcity and containing recommendations designed to bring it to an end.

A decision by the Fund to apportion a scarce currency shall operate as an authorization to a member country, after consultation with the Fund, temporarily to restrict the freedom of exchange operations in the affected currency, and in determining the manner of restricting the demand and rationing the limited supply among its nationals the member country shall have complete jurisdiction.

8. Management.

The Fund shall be managed by a Board of Directors and Executive Committee representing the members.

The distribution of basic voting power shall be closely related to quotas, but no member shall be entitled to cast more than one-fifth of the aggregate votes.

All matters shall be settled by majority, except that a change in the basis of determining quotas shall require a four-fifths vote, and no member's quota may be changed without its assent.


(i) A member country may withdraw from the Fund by giving notice in writing.

(ii) The reciprocal obligations of the Fund and the country are to be liquidated within a reasonable time.

(iii) After a member country has given notice in writing of its withdrawal from the Fund, the Fund may not dispose of its holdings of the country's currency except in accordance with the arrangements made under (ii) above. After a country has given notice of withdrawal, its right to utilise the resources of the Fund is subject to the approval of the Fund.

10. Obligations of Member Countries.

(i) Not to buy gold at a price above the parity of its currency, nor to sell gold at a price below the parity of its currency.

(ii) Not to use the Fund's resources to meet a large or sustained outflow of capital, and the Fund may require a member country to exercise controls to prevent such use of the resources of the Fund. This provision is not intended to prevent the use of the Fund's resources for capital transactions of reasonable amounts required for the expansion of exports or in the ordinary course of trade, banking or other business. Nor is it intended to prevent capital movements which are not out of a member country's own resources of gold and foreign exchange, provided such capital movements are in accordance with the purposes of the Fund.

(iii) Subject to 7 below, a member country may not use its control of capital movements to restrict payments for current transactions or to delay unduly the transfer of funds in settlement of commitments.

Notwithstanding 8 (iii) below, such a change shall require the approval of all member countries with 10 per cent. or more of the aggregate quotas.
countries (other than those involving capital transfers or in accordance with 7 above) or to engage in any discriminatory currency arrangements or multiple currency practices without the approval of the Fund.

11. Transitional Arrangements.

(i) Since the Fund is not intended to provide facilities for relief or reconstruction or to deal with international indebtedness arising out of the war, the agreement of a member country to provisions 4 (c) and 10 (iii) above shall not become effective until it is satisfied to us at its disposal to facilitate the settlement of balances of payments differences during the early post-war transitional period by means which will not unduly encumber its facilities with the Fund.

(ii) During this transition period member countries may maintain and adapt to changing circumstances exchange regulations of the character which have been in operation during the war, but they shall undertake to withdraw as soon as possible by progressive stages any restrictions which impede multilateral clearing on current account. In their exchange policy they shall pay continuous regard to the principles and objectives of the Fund, and they shall take all possible measures to develop commercial and financial relations on terms with other member countries which will facilitate international payments and the maintenance of exchange stability.

(iii) The Fund may make representations to any member that conditions may be favorable to the withdrawal of particular restrictions or for the general abandonment of restrictions inconsistent with 10 (iii) above. Not later than three years from the coming into force of the Fund, any member will retain any restrictions inconsistent with 10 (iii) shall consult with the Fund as to their further retention.

(iv) In its relations with member countries, the Fund shall recognize that the transition period is one of psychological moment, and in deciding on its attitude to any proposals presented by members, shall give the member country the benefit of any reasonable doubt.

ANNEX B.

COMMERCIAL POLICY.

1. In the main body of this report (Section 1) reference has been made to the commitments which have been incurred under Article VII, and to the Cabinet decisions which have already been reached on these commitments can best be met. The problems of commercial policy raised at Washington must be judged against the background of these commitments and previous Cabinet decisions.

I.—THE TRANSITIONAL PERIOD.

2. The discussions at Washington turned primarily upon the long run. Little detailed study was made of the special problems of the immediate post-war period, although—as the following section of the joint Anglo-American document on commercial policy shows—there was full realisation that exceptional measures will be necessary:—

"In the emergency period during and immediately following the war import prohibitions and quantitative limitations would be permitted when necessary to meet emergencies arising from (a) the necessity of rationing imports because of shortages of supplies, shipping or foreign exchange, and (b) a temporary surplus of stocks of the commodity to which the restriction applies. These temporary exceptions would be applicable for a specified limited period after the cessation of hostilities unless the period of their application were further extended by action of the proposed international commercial policy organisation."

Before further progress can be made, the Cabinet must consider how these and other exceptional transitional measures should be applied.

3. The central question is: On what conditions and at what date should the obligations of the proposed commercial convention come into operation? One important condition is that a sufficient number of the commercially important countries should adhere to it. It might be unwise for us to bind ourselves to far-reaching obligations in a convention to which the United States and other important countries were not parties (even though we did not extend the advantages of the convention to non-member States). It might, therefore, be wise to make the coming into force of the convention conditional upon its ratification by a number of States sufficient on the basis of pre-war figures to account for an agreed proportion of total world trade.

4. If the United States and the United Kingdom reach agreement, there will be very strong forces at work to induce other countries to join in. Canada, we know, is anxious to join. Some other countries (such as the "Oso Group," covering Sweden, Norway, Denmark, the Netherlands and Belgium) will certainly wish to adhere. The ex-enemy States can be required to join. The countries so far listed above accounted, with their colonies and dependencies, for no less than 50 per cent. of total world trade in 1938. Many other countries would in such circumstances easily be persuaded to join because of the disadvantages of staying out of so extensive a "low tariff" club.

5. There are a number of reasons for agreeing the convention as early a date as possible. The favourable close of the "war period" may be lost if disputes of difficult points of detail are long postponed after the war. A long period target of sanity is required to influence the commercial policies of the transitional period. Moreover, it will be desirable to set up an international commercial policy organisation at an early date, since an effective international secretariat cannot be built up overnight, and (as is suggested in the next paragraph) an international organisation will be needed to provide a focus for exchange of information and views on with other commercial policy arrangements and their progressive adaptation to the Commercial Union scheme.

6. But if the convention is agreed at an early date, it must expressly provide for exceptional transitional arrangements. The transitional period itself might fall into two parts:—

(i) During the first phase, the international commercial policy organisation would be set up, but member countries would not be bound by the obligations of the convention limiting their protective and discriminatory actions. They would remain free to control their trade in any exceptional way deemed necessary during the immediate post-war dislocation. But they might properly be required to consult with each other through the machinery of the international organisation, on the best means of avoiding mutually injurious measures during this period, and of so arranging the exceptional measures that they led as readily as possible into the long-run arrangements envisaged under the convention.

(ii) There would follow a second phase of a specified duration during which member countries would proceed under defined steps towards the final objective. During this phase, tariffs would have to be
reduced preferences margins to be narrowed, and quotas enlarged, by specified limits each year until the full obligations of the convention were in force.

7. **How should the duration of these transitional arrangements be determined?** There are, broadly speaking, two ways:

(i) The duration of these periods might be named in the convention itself. Thus, the first period might be defined as lasting (say) two years from the adoption of the convention, and the subsequent phase as covering the next (say) three years. Such an arrangement would have the advantage of setting a definite target for the full application of the convention; and it would not preclude the possibility of prolongation of these phases if there were agreement among States covering a sufficient volume of world trade. (See paragraph 3 above.)

(ii) Alternatively, the convention might have defined the length of the first phase. In this case it might be possible to arrange that agreement among States covering on the basis of pre-war figures some agreed proportion of world trade (paragraph 3 above) would be required to bring the second phase into operation. If this proportion were high enough, it would be virtually certain that the second phase could not start without our agreement. For only our own war trade accounts for a large part of total world trade; but our example in such a matter would be followed at least by the devastated countries in Europe which will require time for their own reconstruction and very probably by many other countries as well.

8. Arrangements of the kind suggested above would leave us free to regulate our imports and to encourage or control our exports by any devices, however "discriminatory" or "protective," during the first transitional period, and would provide a subsequent period of gradual adaptation and relaxation. We should, of course, in any case retain indefinitely the opportunity to control our imports on grounds of a balance of payments difficulties, since this is contemplated as a permanent feature of the convention. Moreover, if the second alternative suggested in the preceding paragraph were adopted, we should retain the minority right to prolong the exceptional measures of the transitional period as long as we considered this necessary.

9. The criticism that the commercial policy arrangement discussed at Washington will unduly hamper our internal economic policy, cannot, on examination, be sustained. On the contrary, if we can persuade the Americans finally to accept them, they should positively help us in achieving internal economic stability. One of our chief concerns after the war will be to maintain conditions for the promotion of productivity, prices and incomes. An unfavourable balance of payments may be generated or prolonged, if we successfully maintain our prices and purchasing power while there is a general decline in economic activity elsewhere. The proposals made at Washington (paragraph 3 above) would be of far higher importance than the Ottawa agreements, from 44½ to 48 per cent. But this was also the period in which tariffs (such as the American Hawley-Smoot tariff) and quantitative restrictions were imposed or intensified all over the world; and although the proportion of our trade with the Empire rose, such was the total decline of our exports that this larger proportion of our exports represented a smaller absolute value. Our exports to Empire markets fell from £324 million in 1929 to £322 million in 1937.

10. On balance the Washington proposals should greatly help us to expand our export trade by limiting the barriers raised against our exports. To a country which imports essentials and exports manufactured goods which take second place, the selection of the exports we are to use, a general clearance of the channels of trade is of first-rate importance. The favorable effect upon our export trade would be offset to some extent by the loss, at least in part, of the preferences which our exports at present enjoy in Empire markets. But the effect of such preferences should not be exaggerated. Between 1929 and 1937 (both years of high world economic activity) the proportion of our exports which went to Empire markets rose, in the result of the Ottawa agreements, from 44½ to 48 per cent. But this was also the period in which tariffs (such as the American Hawley-Smoot tariff) and quantitative restrictions were imposed or intensified all over the world; and although the proportion of our trade with the Empire rose, such was the total decline of our exports that this larger proportion of our exports represented a smaller absolute value. Our exports to Empire markets fell from £324 million in 1929 to £322 million in 1937.

11. The United Kingdom tariff is of moderate height. We have to sell our exports in the United States and in many other overseas markets over much higher duties. A multilateral convention to reduce tariffs all round, but to reduce high tariffs more drastically than moderate tariffs could greatly help us by reducing the barrier to our exports without imposing on us any comparable reduction in our duties. To take one example, between 1929 and 1937 (both years of high internal purchasing power in the United States) the value of our exports in the United States (excluding Empire) was £31.4 million or by 91 per cent.; and this must be largely ascribed to the Hawley-Smoot tariff which was imposed in 1930, even though its excesses had in some respects been modified by Mr. Hull's Trade Agreements.

12. But above all our exports suffered after 1930 from the proliferation of import restrictions which were imposed on them in overseas markets. More than twenty countries before the war had imposed restrictions on our exports, and these restrictions covered the importation of many of our important products into many of our important markets. Our exports to a selection of countries (namely, Bulgaria, France, Germany, Greece, Hungary, Italy, Latvia, Poland, Roumania, and Switzerland) fell from 1929 to 1937 by no less than 38½ per cent. (More evidence of the effect of the Washington proposals on our export opportunities is provided in paragraphs 29 to 26 of W.P. (44) 75.)

13. In return for this clearance of barriers against our exports, our freedom to protect particular industries and occupations in this country would, of course, be circumscribed. Any discussions about "action directed towards the reduction of tariffs and other trade barriers" which did not imply this would, of course, be a mere farce. Nevertheless, the proposals discussed at Washington leave reasonable allusion for the protection of particular industries. First, there is no proposal to eliminate tariffs. And the tariff proposals which we can seriously discuss all have one thing in common; they involve a more radical cut in high than in low tariffs. We would be required to cut our tariffs less than other countries with high tariffs, and we would be able to impose new tariffs or to revive existing tariffs on anything which we wished to protect, up to a certain moderate level. Secondly (although, as explained in 17 (ii) above, agreement has not been reached on this topic with the Americans), our officials at Washington have insisted that the freedom to pay direct and disguised subsidies to any particular industry must be preserved.

14. There seems to have been some misunderstanding about the implications of the proposals on
State-trading, which were accepted by the American officials at Washington. These proposals do not hinder us or any other country from monopolising the whole of its foreign trade or from conducting a mixed system of State-trading in certain commodities and private trade in others. No country would be deprived from introducing greater stability into its international commerce by long-term State-contracts for its imports or exports. On the other hand, an attempt has been made to avoid the use of State-trading mechanisms merely to re-introduce by another means the protective and discriminatory mechanisms which are to be barred under other clauses of the convention.

The Washington proposals do not attempt to judge between State enterprise, private enterprise, or mixed systems of trading; they try merely to set some limit to the protective and discriminatory use of each of these systems.

15 The Washington proposals do suggest that countries should not set up State-trading monopolies merely in order to cover their trade with a State-trading country, where no State monopoly is set up to cover their trade in the same commodities with private enterprise countries. This is a limited issue which it might be wise to treat separately from the main issue (paragraph 17 (v) below).

16 It may be useful to see how these arrangements would circumscribe our policy for any particular industry—for example, agriculture:

(i) Quantitative restrictions on our imports of agricultural products would be ruled out as a normal means of agricultural protection, though they could be employed during the transitional period, during periods of severe strain on our balance of payments, or as part of an international commodity arrangement.

(ii) Moderate tariff protection up to a limited additional ad valorem level would be permissible on any products.

(iii) Direct subsidies, with or without such limited tariff protection, would be permissible to an unlimited extent, if the view put forward by our officials at Washington were to prevail. The American officials wished to set some limit to the subsidisation of commodities in world surplus supply. If the compromise solution suggested in paragraph 17 (iii) below were adopted, we could be under an obligation to enter into ad hoc discussions in each case on the possibility of limiting such subsidisation but would retain our ultimate right to continue what subsidies we considered necessary.

(iv) Schemes involving a levy on imports, the proceeds of which are payable as a subsidy to home production, would be allowed provided that the levy did not exceed the level permitted by the tariff rule.

(v) The trade in any commodity could be monopolised by the State.

Subject to a satisfactory solution of the subsidy issue, the proposals would thus allow protection to any degree, provided that any protection in excess of the level permitted by the tariff rules was given by means of subsidy. They would, moreover, permit (whether by means of levy, subsidy arrangements or by State-trading arrangements) the payment of guaranteed prices to any agricultural product, provided again that any protection in excess of the margin set by the tariff rules was given by raising the price to the consumer by means of a direct charge on the Rouble.

17. Questions Requiring Further Cabinet Decision.

(i) Transitional Arrangements.—It is necessary to consider whether arrangements for the transitional period on the lines indicated in paragraph 2-8 above should be put forward by the Dominions and subsequently in further discussions with the Americans, it will be necessary for the Cabinet to give some guidance to our officials on a number of points. General Ministerial guidance on these matters is necessary. But precise decisions would be out of place since at the next stage of official discussions with the Americans frequent reference by officials to Ministers will certainly be necessary as these question are put forward in the following lines:

(ii) Tariffs and Preferences.—American officials at Washington made it clear that a really drastic reduction of the American tariff would be out of the question except in return for an equally drastic reduction of high tariffs achieved by alternative means would justify the practical elimination of imperial preference. The final fulfilment of Article VII might be achieved in two stages on each side; in this case, it is for consideration whether, as the first stage, we should contemplate a somewhat more moderate reduction of high tariffs in return for a less drastic reduction of the American tariff. (See paragraph 7 (c) of Annex C of this report.) A solution might perhaps be found on the following lines:

In the case of commodities declared by some agreed procedure to be in world surplus supply, the rule against export subsidies would lapse unless an ad hoc agreement were reached to limit subsidies on production. Such an arrangement would enable us to retain the ultimate right to subsidise our home production as much as we considered necessary, but would restrain the payment of export subsidies on manufactured goods (such as the pre-war German subsidies from which our export trade suffered severely).

(iii) Subsidies.—The American officials at Washington agreed in principle to the abolition of export subsidies. But they maintained that in the case of commodities in world surplus supply (such as wheat and cotton) they could not do so unless some limit were also set to the subsidisation of production of these commodities in other countries. The United Kingdom officials maintained that the right to subsidise total production should not be limited. The some divergence of view revealed itself in the Washington talks on commodity arrangements. (See paragraph 7 (d) of Annex C of this report.) A solution might perhaps be found on the following lines:

In the case of commodities declared by some agreed procedure to be in world surplus supply, the rule against export subsidies would lapse unless an ad hoc agreement were reached to limit subsidies on production. Such an arrangement would enable us to retain the ultimate right to subsidise our home production as much as we considered necessary, but would restrain the payment of export subsidies on manufactured goods (such as the pre-war German subsidies from which our export trade suffered severely).

(iv) Infant Industries and Industries Necessary—Grounds of Security.—The American officials argued that any protection required by such industries, additional to that permitted under the tariff rules, should be provided by subsidies. The acceptance of the obligations of the convention by undeveloped countries was, however, considerably facilitated if some higher level of tariff protection were permitted in these cases. For this reason, it might be wise to devise a properly safeguarded tariff exception, which in the case of infant industries would be of a temporary character.
The Position of Non-Member States.—Canadian officials in the talks held in London last June and American officials in the recent talks at Washington have urged that the tariff benefits derived from the proposed convention should not be extended to those countries which were not willing themselves to accept the same obligations. In order to induce as many countries as possible to subscribe to the convention this would probably be as wise as it is equitable. In the case of an Empire country which did not participate, there would have to be changes in the treatment of its trade which would ensure that it was certainly not more favourably, and probably less favourably, treated than that of participating Empire countries. If this contingency should arise, the matter would clearly have to be dealt with by some sort of modus vivendi.

(vi) Counter-Monopoly for Trade with Russia.—The Americans at Washington urged that State-trading monopolies should not be set up merely to monopolise that part of a country's trade which was under-taken with another State-trading country (though they fully admitted the right of any country to monopolise its trade with all other countries either for particular commodities or for all commodities). The problem which will come up shortly for Ministerial decision in another connection.

ANNEX C.

COMMODOITY POLICY.

His Majesty's Government is bound by no exactments in regard to Commodity Policy. It is an Article VII of the Atlantic Charter states that the United States and the United Kingdom—

does not have the obligation to consider what its trading monopolies should not be set up merely to monopolise that part of a country's trade which is undertaken with another State-trading country (though they fully admitted the right of any country to monopolise its trade with all other countries either for particular commodities or for all commodities).

Moreover, the recommendations of the Hot Conference, which have been accepted in the Charter save in 'so far as it rules out another connection.

However, from certain discriminatory duties on products from Malay and Nigeria and for a period on palm oil exports from Nigeria, there are no discriminatory sales of primary products inter-war period from the United Kingdom and use under its control. In general, therefore, these can only relate to the desirability of such discriminatory arrangements in regard to commerce as may make it more difficult for countries to acquire the foreign exchange to purchase the primary products they use. Policy, as such, is not affected by the Charter save in so far as it rules out monetary sales in the future.

To quote from the Atlantic Charter:

Article VII obliges us to seek measures to further the enjoyment by all great and small, victor or vanquished, of access on equal terms to the trade and to the raw and manufactured products which are needed for their economic prosperity.

But the knowledge that His Majesty's Government are disposed to treat it as a last rather than a first resort would give a lead to the Department to explore alternative methods of dealing with the situation (e.g., the freeing of Government-owned stocks of metal so as to clear the outlets for new production) and to discuss them with producers.

Secondly, there are two commodities—rubber and sugar—which are still in acutely short supply but which claim attention for another reason. Each of them is the subject of a pre-war regulation agreement which is just about to expire; and in each case the question has arisen whether to renew the agreement as it stands, or to work for the establishment of a broadly-based international committee which, for the time being, would confine itself to intelligence and statistical activities, but which might be expected to develop later into a policy-forming body. These decisions are having to be taken as a matter of urgency in an attempt to keep the situation fluid pending the formulation of long-range Government policy in this field; but if our representatives on the bodies dealing with these commodities are to function effectively, it will be necessary for them to receive guidance at no distant date as to what that policy is.

6. Other instances of each of these two groups of cases are likely to emerge during the transitional years. It would seem that the sooner an agreed body of principles can be approved, and the sooner a central institution can be set up to which existing regulation schemes or their more flexible successors can be affiliated, the less troublesome these problems will be to handle.
State-trading, which were accepted by the American officials at Washington. These proposals do not hinder us or any other country from monopolising the whole of its foreign trade or from conducting a mixed system of State-trading in certain commodities and private trade in others. No country would be debarred from introducing greater stability into its international commerce by means of long-term State-contracts for its imports or exports. On the contrary, an attempt has been made to avoid the use of State-trading mechanisms merely to re-introduce by another means the protective and discriminatory mechanisms which are to be barred under other clauses of the convention. The Washington proposals do not attempt to judge between State enterprise, private enterprise, or mixed systems of trading; they try merely to set some limit to the protective and discriminatory use of each of these systems.

15. The Washington proposals do suggest that countries should not set up State-trading monopolies merely in order to cover their trade with a State-trading country, when no State monopoly is set up to cover their trade in the same commodities with private enterprise countries. This is a limited issue which might be wise to treat separately from the main issue (see paragraph 17 (vi) below).

16. It may be useful to see how these arrangements would circumscribe our policy for any particular industry—for example, agriculture:

(i) Quantitative restrictions on our imports of agricultural products would be ruled out as a normal means of agricultural protection, though they could be employed during the transitional period, during periods of severe strain on our balance of payments, or as part of an international commodity arrangement.

(ii) Moderate tariff protection up to a limited and fixed level would be permissible on any products.

(iii) Direct subsidies, with or without such limited tariff protection, would be permissible to an unlimited extent, if the view put forward by our officials at Washington were to prevail. The American officials wished to see some limit to the subsidisation of commodities in world surplus supply. If the compromise solution suggested in paragraph 17 (iii) below were to be adopted, we would be under an obligation to enter into ad hoc discussions in each case on the possibility of limiting such subsidisation but would retain our ultimate right to subsidise total production should we consider necessary.

(iv) Schemes involving a levy on imports, the proceeds of which are payable as a subsidy to home production, would be allowed provided that the levy did not exceed the level permitted by the tariff rule.†

(v) The trade in any commodity could be monopolised by the State. Subject to a satisfactory solution of the subsidy issue, the proposals would thus allow protection to any degree, provided that any protection in excess of the level permitted by the tariff rules was given by means of subsidy. They would, moreover, permit (whether by means of export duties or ad valorem by State-trading arrangements) the payment of guaranteed prices to any agricultural product, provided again that any protection in excess of the margin set by the tariff rules was given not by raising the price to the consumer but by means of a direct charge on the Exchequer.

† If, for example, the rule suggested tentatively by our officials at Washington were accepted, this would permit in all cases a levy of 25 per cent on imports. No levy above 25 per cent would be permitted in any case. The basis of treatment of new duties or levies between these two levels has still to be determined.

III.—QUESTIONS REQUIRING FURTHER CAREFUL DECISION.

17. If the general line of commercial policy dictated at Washington is to be considered further, first, forthwith, with the American officials at Washington. These proposals do not attempt to judge between State enterprise, private enterprise, or mixed systems of trading; they try merely to set some limit to the protective and discriminatory use of each of these systems.

(i) 

111..—Questions Requiring Further Careful Decision.
The Position of Non-Member States—Canadian officials in the talks held in London last June and American officials in the recent talks at Washington have urged that the tariff benefits of the proposed convention should not be extended to those countries which were not willing themselves to accept the same obligations. In order to induce as many countries as possible to adhere to the convention this would probably be as wise as it is equitable. In the case of an Empire country which did not participate, there would have to be changes in the treatment of its trade which would cause that country to be certainly not more favourably, and probably less favourably, treated than that of participating Empire countries. If this contingency should arise, the matter would clearly have to be dealt with by some sort of mutual agreement.

(vi) Counter-Monopoly for Trade with Russia.—The Americans at Washington urged that State-trading monopolies should not be set up merely to monopolise that part of a country's trade which was undertaken with another State-trading country (though they fully admitted the right of any country to monopolise its trade with all other countries either in specific commodities or in all commodities). This is an issue which will come up shortly for Ministerial decision in another connection.

ANNEX C.

COMMODITY POLICY.

1. His Majesty's Government is bound by no exact commitments in regard to Commodity Policy. It is true that Point 4 of the Atlantic Charter states that the United States and the United Kingdom—

"will endeavour, with due respect for their existing obligations, to extend the enjoyment by all States great and small, subject to equitable, rules on which Commodity Policy might be based. No very general terms, the creation of an international commodity organisation and the outline of a code of conduct for general economic prosperity."

Apart, however, from certain discriminatory duties on exports from Malaya and Nigeria and (for a temporary period) on palm oil exports from Nigeria, there were no discriminatory sales of primary products in the inter-war period from the United Kingdom and territories under its control. In general, therefore, this clause can only relate to the desirability of avoiding such discriminatory arrangements in regard to finance and commerce as may make it more difficult for some countries to acquire the foreign exchange necessary to purchase the primary products they use. Commodity Policy, as such, is not affected by the Atlantic Charter save in so far as it rules out discriminatory sales in the future.

2. There are, however, certain indirect commitments. Article VII obliges us to seek measures conducive to general economic expansion; it may be held, therefore, that attempts on the part of some countries to seek for an international code in respect of Commodity Policy, which would facilitate the achievement of this goal. Moreover, the recommendations of the Hot Springs Conference, which have been accepted in principle by His Majesty's Government, contain a resolution on Commodity Policy suggesting, it is true in very general terms, the creation of an international commodity organisation and the outline of a code of rules on which Commodity Policy might be based. No precise obligation is implied in all this, but inasmuch as arrangements made or contemplated in regard to important commodities entering international trade may directly affect general measures for economic expansion, it is incumbent on us to consider what our general policy should be in regard to such arrangements and to ensure that it does not conflict with the broad objects of Article VII.

I.—THE TRANSITIONAL PERIOD.

3. In so far as they related to Commodity Policy, the discussions at Washington were concerned exclusively with the outline of a possible permanent settlement. No special attention was given to problems of the transition.

4. The problems of transition which have hitherto arisen are of two kinds. In the first place, there are certain war metals—copper and aluminium are the leading examples—of which surplus supplies are certain to emerge at a very early date. In the case of these commodities it is urgent that Departments should have some guidance as to the long-run objectives of Government policy and the possible remedies for conditions of over-supply. In the case of certain war metals—their economic policy which His Majesty's Government made which would prove to run counter to the general policy should be in regard to such arrangement...
The principal organ of the international commodity organisation would be a general commodity council, operating for purposes of day-to-day business through a general executive. Votes in the council would be allocated among members on an appropriate basis, account being taken of their share in international trade.

Control of particular commodities would be devolved on individual commodity organisations, and it would be a fundamental principle that, in the composition of any such organisations, "countries largely dependent upon imports of supplies of the particular commodity in question should have a combined vote equal to the exporting countries."

Under the agreement proposed, participating States would retain the right of final decision regarding proposed international commodity arrangements. The organisation would help to form such arrangements, and would review and report upon them before they were submitted to Governments for conclusion. The Governments would undertake that any arrangements not so initiated should be communicated in full detail to the international organisation. But in the last analysis they would retain freedom of action.

Provision is made in the agreed statement both for buffer stock arrangements and for quantitative regulation. It is agreed that the latter is to be regarded as a "transitory" expedient, to be introduced only where there is persisting disequilibrium between supply and demand which may necessitate special measures for the protection of producers and the facilitation of orderly change. It is agreed that, where quantitative regulation of exports or production is proposed, there should be special safeguards in order to ensure that the fundamental objectives of international Commodity Policy are not infringed:

(i) Equal representation of producers and consumers.
(ii) Full exploration of alternative measures for dealing with the root causes of the disequilibrium between supply and demand.
(iii) The obligation to make provision for increasing opportunities for supplying world requirements from the sources of low-cost production.
(iv) No quantitative regulation scheme to be approved for more than five years, or to be renewed save upon endorsement by the general executive that the above principles, particularly those at (ii), have been observed.

It is not possible to predict at this stage what would be the relative importance of the different types of policies permitted. It became clear in the course of the discussions that differences of opinion on this subject related much more to differences of view on the prospects of the commodity markets than to differences of view on the ultimate principles involved. If we adopted the proposed agreement we should be free to argue each case on its merits. And we should be assured that, if circumstances compelled us to admit that there was justification for quantitative regulation, this would take place under conditions in which, as consumers, we had adequate representation, and were subject to the safeguard that artificial arrangements permanently protecting high-cost production were ruled out.

It is proposed that the Permanent Organisation for Food and Agriculture should be organically linked with the international commodity organisation by representation on some Government body.

There is a difference of view regarding subsidies. The Americans suggest that where subsidies were allowed in respect of commodities suitable for international regulation, they should be accompanied by quantitative limits on the amount of subsidised production. This cuts across our proposals regarding Commercial Policy, where the use of the subsidy as a safety-valve is one of the main principles of the scheme. This is the one outstanding point of difference between ourselves and the Americans at the moment. And it is probable that the Americans, who wish in this way to reduce their own commitments regarding subsidies, will press us hard. A possible line of compromise is suggested in paragraph 17(iii) of Annex B of this report.

8. Before the matter can be further pursued, in conversations with the Dominions and perhaps, at a later stage, with the Americans, certain broad decisions by Ministers are required. The following are the main questions on which such decisions are necessary:

(a) Do Ministers consider that—having regard, as the one had, to the broad issues of policy involved, and, on the other, to our responsibility for Colonial producers—the main approach in the paper to commodity arrangements should be the broad objective of His Majesty's Government? In other words, are Departments to operate in the knowledge that His Majesty's Government would wish that quantitative regulation schemes to be avoided in the first place and to be used only as a last resort to deal with position of persisting disequilibrium between supply and demand, and then to be made subject to the safeguards indicated in the statement of principles?

(b) If the answer to (a) is in the affirmative, are Ministers prepared to agree that the Permanent Organisation for Food and Agriculture should be an organic part of the new international commodity organisation?

(c) Should we work towards the ultimate establishment of an international commodity organisation on the lines indicated in the statement of principles?

(d) If an international commodity organisation is established, are Ministers prepared to agree that His Majesty's Government should accept the obligation to refer to it for scrutiny and report any commodity schemes to which they or their nationals may be parties or may hereafter become parties?

(e) What line is to be adopted in regard to the subsidy question? Would a compromise on the lines suggested in the section on Commercial Policy be acceptable?

(f) Is it agreed that there should be created the link proposed between the international commodity organisation and the Permanent Organisation for Food and Agriculture?
ANNEX D.

CARTEL POLICY.

1. The American officials at Washington raised the problem of international cartel agreements. There are important sections of American official opinion which enjoy and, even with a change of Administration, would probably continue to enjoy the support of Congress and of public opinion, which feel very strongly about the need to restrain the anti-social practices of international cartels. Some of the evidence which the American officials put before our officials on this subject was impressive in itself; and it is difficult to find an answer to the American argument that we should not permit private producers or merchants, by private and uncontrolled agreements, to reintroduce those obstacles to the flow of trade which is proposed to limit or to outlaw by Government action under the Commercial Policy arrangements.

2. Our own officials had no instructions on this subject and were, therefore, compelled to adopt a passive role and to listen to the American proposals. These proposals go considerably beyond the mere suggestion that international cartel arrangements should, by international agreement, be subject to registration with some international body. They envisage rather an elaborate code of rules for the outlawing of many cartel practices. It is very doubtful whether we should wish to go as far as the Americans in this policy. We have still to decide whether our interest lies. Can we hope to gain by the maintenance of the price of some of our exports and by the protection of some of our markets which cartel agreements may bring us? Or would such agreements tend rather to be too restrictive for a country which must be free by one means or another to expand the volume of its exports perhaps some 30 per cent, above the pre-war level? Can we hope successfully to resist American pressure for an anti-cartel policy and, at the same time, to maintain a policy directed against restriction schemes for the primary products which we import?

3. Our answers to these questions must, no doubt, depend largely upon the internal policy which we adopt generally in regard to restrictive practices in industry, and which Ministers have now under consideration. In particular, do internal cartel arrangements, by organising large-scale production and by preventing unnecessary price competition among our exporters, help to promote the value of our exports? Or do they, by maintaining the cost of the materials and components of our manufactured exports, impair our competitive position?

4. We need much factual information before we can decide these issues. The President of the Board of Trade is already, I understand, carrying out an enquiry on these lines, and, in the light of the facts which are thus disclosed, we must decide what line of policy to adopt. In any case, we must not deceive ourselves about the importance of this topic if we wish to reach agreement with the Americans on the wide range of international economic problems. If we show undue reluctance to enter, at the appropriate time, into further discussion on international cartels, we run grave risk of prejudicing further progress in the fields of Commercial Policy and Commodity Policy.

ANNEX E.

EMPLOYMENT POLICY.

1. This was a subject which the Americans raised, and since the broad lines of our own internal policy for the maintenance of employment was at that time still undecided, it was not possible for the United Kingdom officials to enter into any detailed exchange of views on internal employment policies. However, the various specialised international economic institutions which have been proposed (such as the monetary organisation, the investment bank, the commodity organisation and the commercial policy organisation) all may exercise an important influence over general economic expansion throughout the world, and so over the opportunities for employment in the various countries of the world. Apart from this, the internal policies of the major countries of the world through their success or failure to maintain a high level of internal economic activity, react in an important way upon the opportunities for employment in other countries.

2. In effect, therefore, the international aspects of employment policy are concerned either with the co-ordination of the activities of other specialised international institutions or with the provision of opportunities for the exchange of views and information between countries on the different internal economic policies which they have pursued for the maintenance of employment. The Washington talks on this subject concentrated accordingly on the possibility of instituting, for this and kindred purposes, some central international economic organisation, served by an economic advisory staff.

3. It is probable that the Australians at the forthcoming Dominions talks will lay great emphasis, as they did during the Dominions talks in London last June, on the need for international policy for the maintenance of economic activity and employment. It is, therefore, necessary to decide whether the United Kingdom officials in forthcoming talks with the Dominions should be authorised to pursue further the possibility of a central international economic organisation of this character.
ANNEX F.

INTERNATIONAL INVESTMENT.

1. The Americans at Washington took the initiative in laying before our officials a draft project for an international bank to promote long-term international investments. This subject did not, however, form part of the official discussions at Washington, since the United Kingdom officials had no instructions on the subject which was raised by the Americans only towards the end of our visit. The matter is, however, one which is closely allied to the proposals for the international monetary organisation. It is also one which might have considerable importance from our point of view. If the United States is destined to have a very favourable balance of payments, it is important that she should match this with long-term capital movements to the countries most in need of capital development; and such lending would be above all useful to us in so far as the principle could be accepted that the expenditure of long-term loans should not be tied to the products of the lending country. Moreover, any action which promoted the planning and timing of international investment in such a way as to maintain economic activity at a stable level, might be of considerable use in a general policy for the maintenance of economic activity and of employment. On the other hand, of course, it would not be appropriate for a country in the position of the United Kingdom, with the prospect of a difficult balance of payments problem, to commit itself in advance to provide any considerable funds for international investment. It is for the countries with favourable balances to lend abroad.

2. Whether or not the American proposals allow for, or could be made to allow for, these principles, is a matter for expert consideration. Indeed, the whole subject requires technical consideration at the official level before Ministerial decisions can usefully be received upon it. But the topic has already been raised by the Americans and is likely to be raised by them again; and it is one in which we have a vital interest at stake. I would, therefore, propose that the Chancellor of the Exchequer should be invited to arrange for an examination of the American proposals by the Treasury in consultation with the other Departments primarily concerned and to report upon them to the Cabinet.