WAR CABINET.

BRITISH EXPORTS, GERMAN INDUSTRY AND REPARATIONS.

MEMORANDUM BY THE PAYMASTER-GENERAL.

At first sight there appears to be a conflict of interest over the rebuilding of German industry. The smaller her industry, the smaller will be her war potential; but the smaller her industry, the smaller also will be the reparations which can be extracted in the form of manufactured goods. As far as this country is concerned, this apparent conflict is, in my opinion, unreal. From the British point of view, the slower the recovery of German industry, the better. True, we shall not get manufactured goods as reparations. But we shall get what is infinitely more valuable to us, namely, a considerable share of Germany's pre-war export markets.

I.—Our Export Problem.

For two years now the value of our imports (not counting munitions) has been five times the value of our exports. In other words, a large part of the food we eat at every meal, and of the raw materials used daily in industry, are gifts or loans from abroad.

Nearly half our imports are on Lend-Lease or Mutual Aid from North America; when the war is over these gifts will cease. Much of the other half is on credit from other countries; as we have borrowed so much from them already, we can hardly expect them to go on lending to us indefinitely when the war is over.

Merely to pay for food to keep ourselves alive, and for materials to keep our factories running, we must expand our present-day exports five times—and that in a very short time if we are to avoid becoming pensioners of North America.

Ever since 1913 there has been an ominous downward trend in our exports (after allowing for price changes). By 1938, although the rest of world trade had increased, and the world demand for industrial products had risen by well over one-half, our exports had fallen to less than two-thirds of the 1913 level. During this war they have perforce been cut to less than one-third of even the 1938 volume. In face of all the wartime industrialisation that has taken place in Canada, Australia, India, Brazil and other countries, and of the infiltration of American products throughout the world, it will be difficult enough to regain our 1938 markets. But this will not suffice. Somehow or other we must in addition reverse the sinister decline that had been afflicting our exports for a generation even before this war, and raise them in the course of a few years to one and a half times the 1938 level—a truly gigantic task.

And yet we must succeed if our plans for full employment and social reform are to be anything but a mirage, and if the influence we hope to wield in the world is not to be paralysed by dependence on our creditors and shortage of cash.

II.—The German and Japanese Export Markets.

Our biggest opportunity lies in the capture of the German and Japanese export markets. Before the war, in a total world market for finished manufactures of £2,000 million, we supplied goods worth £400 million, the Germans another
£400 million and the Japanese £175 million. Here then is an opening of
tremendous importance. A substantial slice of the enemies' export markets would
go far to solving our problems.

To-day we have a unique opportunity to achieve this. Our two major allies
have shown no exceptional solicitude for the future of German industry, and we
shall soon be occupying the most important industrial area in Germany, devastated
by bombing and the ravages of war.

If we decide to forgo this opportunity, if we decide that German industry
and exports must be restored, let it be plain what this means to Britain. Quite
apart from questions of military security, it means deliberately throwing away
the largest single chance we have of restoring and expanding our exports, without
which we are condemned to poverty, penury, debt and decline. Only very
compelling reasons could justify His Majesty's Government in taking
responsibility for such a policy.

III.—Two Immediate Issues.

A decision on these matters cannot be postponed. Two questions demand
immediate answers:—

(a) As soon as we have occupied the Ruhr there will be pressure from many
quarters to restore its industry. It will be argued that the Germans
must send manufactures to their neighbours in payment of the repara­
tions which are their due; that they must export in order to pay for
their necessary imports; that their factories must be restarted if mass
unemployment, with all its social and political implications, is to be
avoided.

There are answers to these arguments, and they are set out below. Here I am only concerned to emphasise that, if we accede to these
demands, we shall not only be resuscitating our principal pre-war
competitor in the export market; we shall have to restock and
re-equip German factories largely out of our own pocket (at any rate
until we can be recouped by the recipients of reparations—at some
uncertain future date); we shall no doubt have to contribute brains
and effort which we can ill spare from the task of getting our own
industry going; and we shall be helping the Germans to make for
the European Allies, free of charge, manufactures which they would
otherwise have bought from us for cash—gold and foreign exchange
which we cannot afford to forego.

I therefore trust that we shall do nothing to encourage the
rebuilding of German industry, at least without very carefully
counting the cost.

(b) The second immediate question arises out of the appointment of a
Reparations Commission in Moscow. It was clear at Yalta that
neither the Americans nor the Russians had given much thought to
the question; consequently a vigorous lead from Britain on a clear­
cut policy might achieve considerable results. This makes it all the
more necessary to consider very carefully what policy our representa­
tives are to press.

Some of the results of a decision to make Germany pay reparations
in the form of manufactured goods have already been described.
Above all, it would rule out the only German reparations of real
value to us—her export markets. Moreover, although I am dealing
primarily with economic matters, it must not be forgotten that
Germany's capacity to make war follows from her capacity to manu­
facture goods. This should appeal to all the United Nations alike.

In my view it should be possible to reach an agreement with the
Russians by which they would take existing German machinery,
forced labour and raw materials, while we should take German
export markets (and also perhaps certain special types of
existing equipment, and raw materials like timber and potash);
obody would receive any manufactured goods—a policy the
Americans would almost certainly endorse. It is true that this would
involve the sacrifice by this country of reparations in the form of
manufactured goods. But during the first few years, as the
Chancellor of the Exchequer has warned us in W.P. (43) 146, we
cannot hope to get much from Germany anyhow. And once our own factories have been reconverted, it is unlikely that Labour or Capital would welcome a flood of German manufactures. In any event, Britain's share of such manufactures would certainly be worth very little compared with the value to us of German export markets. Some of the other Allies might of course like to have German manufactures, but their preferences must not be allowed to override our vital interests. As the Russians have recognised, the needs of the countries that have organised victory must take first place.

IV.—The arguments for restoring German Industry.

We are not so much faced with the question whether or not to destroy German industry. A large part is, or will be, in ruins. What we have to decide is whether we are to allow and help the Germans to rebuild it.

What compelling reasons might be held to justify our taking a step that would so grievously hamper our export prospects? Certainly not that we need her manufactures as reparations. What other arguments are there? Three of those which are current may be briefly examined.

(a) It is said that there will be mass unemployment in Germany after the war if her industry is not fully restored.

This argument, in my view, usually receives undue weight. The German metal, engineering, electrical and chemical industries are the most important from the export—as from the military—point of view. They accounted for two-thirds of Germany's pre-war exports. But even in 1939, with rearmament in full swing, they employed only 5 million people out of a total working population of 34 million.

It is idle to pretend that a large part of these 5 million could not find work elsewhere. At least 2 million workers will be occupied for five years rebuilding German dwellings damaged or destroyed in the war and in building houses for the Germans to be evacuated from the Eastern territories. Nearly 9 million workers were actively engaged in agriculture in 1925. Between 1925 and 1939 nearly 3 million left the land; they might go back. And if the large estates were broken up, another million workers could be settled on the land. Some 3 million Germans, for whom work would otherwise have had to be found, have been killed in the war. By the time the Germans have met Russian demands for workers to make good the ravages inflicted on their country—a figure of 4 million has been mentioned—there may well be a shortage, rather than a surplus, of man-power in Germany.

Nobody maintains, of course, that the transition from war to peace will be easy in Germany. To demobilise the German Armed Forces (9 million men including prisoners in Allied hands), and to shift perhaps 5 million munitions workers to peaceful pursuits, will tax German organising power to the utmost. Failure to restore German heavy industry may aggravate the inevitable problem of transitional unemployment, but it will hardly affect its order of magnitude. It may be that factory workers would prefer to stand at a bench rather than work on the land or build houses—but the sacrifice of their preferences is not a heavy price to pay for starting the bloodiest war in history.

(b) It has also been said that the Germans' standard of life will be reduced to intolerable levels unless their industry is restored.

This is another of those qualitative statements which does not bear quantitative analysis. For the last five or even ten years, nearly all German heavy industry, and much of her light industry, has been turning out predominantly munitions and warlike stores. A small fraction of this capacity, devoted entirely to peace-time production, would give the Germans far more consumer goods and a higher standard of life than they have had for a long time.

Then it is said that Germany will be unable to export enough to pay for her necessary imports. The operative word here is 'necessary.' Unlike this country, Germany is very nearly self-sufficient in food-stuffs; even at the height of her war effort in 1942-43 she produced enough on her own land to provide a daily average of 2,300 calories per head—nearly nine-tenths of her
total consumption. A relatively small increase in agricultural output would
give the Germans, without any imports at all, as many calories as most other
European countries.

Some fats would have to be imported, and probably a few million tons of
grain to offset territorial losses in the East; but these, together, would not
exceed one-tenth of the total value of Germany's pre-war imports.

As to raw material imports, German civilians have managed for five years
practically raw material less supplies; they have developed many kinds of ersatz
materials, especially textiles. The need for imports of ores and metals will be
greatly reduced if German heavy industry contracts. Thus, there is no doubt that
she could survive with a much smaller industry, and much smaller exports,
than before the war. There would be fewer motor cars and oranges, less coffee
and tea, but the basic essentials of life would be available.

(c) It is argued that failure to restore German industry would impoverish
Europe and the world.

It is of course true, as an abstract proposition, that if productive capacity is
eliminated, fewer goods will be produced than could be made if it remained
intact. But the question now is not whether German factories should be destroyed
or not. They have been destroyed. The question is whether they should be
rebuilt in Germany and employ German labour or whether the goods they could
produce for export should be made here. Nobody seriously expects to get very much
from the output of German factories in the first year or two. After that there
will not be any danger of the United Nations running short of the manufactures
they want. There has been an enormous expansion in manufacturing output
and capacity during the war. For example, the wartime increase in the output
of the British metal, engineering and allied industries has been at least two or
three times as great as the total pre-war export by similar Germany industries.
The increase since 1939 in the output of American factories has been something
like 25 times as great as Germany's total pre-war exports of manufactures; the
expansion of 53 million tons a year in American steel production is 1½ times
Germany's total pre-war output of 22 million tons.

The dependence of European countries on the German market is also apt to
be exaggerated. The industrial countries of the Continent will have no grounds
for complaint. Before the war they sent only 13 per cent. of their exports to
Germany, and they will surely gain on balance by a reduction of Germany's
competitive power; but even if they did not, we must consider our own needs first.

As for the European producers of raw materials and food-stuffs, the only
countries depending on the German market for more than one-fifth of their pre­
war exports, apart from the Baltic States which are now part of Russia, were:—

Bulgaria, Hungary, Spain and Turkey, whose part in the war scarcely
qualifies them for special consideration:

Greece and Yugoslavia, two small allies whose needs we can easily supply
and whose exports of ores and metals, timber, currants and tobacco we can
readily absorb.

As for the overseas countries, practically every one of them, unlike the United
Kingdom, is in a much stronger financial position than before the war and well
able to tide over any losses that might be involved.

As a result of her fight to save liberty, Britain has become the greatest debtor
nation of the world. We have the right to demand that our interests be considered
in the post-war settlement. Let us not forget that a weak Britain, struggling
with unemployment and a low standard of life, her foreign trade reduced and
her exchanges constantly threatened, might well impoverish the world far more
than a contraction in German industry.

V.—Other Arguments.

In this note I have considered only the economic repercussions of our
treatment of German industry after the war. But clearly the more we curtail
her heavy industry, the greater will be our military security. It is comparatively
easy to stop new factories being built. But, once they have been built, it is
notoriously difficult to make sure that they are not diverted to wrong uses.

It has also been argued that a lower standard of life in Germany might tempt
foreign capitalists, despite their experience after the last war, to erect factories
in order to exploit the cheap German labour. Naturally, if it is decided not to
restore German industry until she is fit to resume her place among civilised nations, this must not be allowed. No factories could be erected without special permission.

It is sometimes said that a harsh settlement would be resented by the Germans and would stimulate a war of revenge. But surely no one who has lived through the past ten years still believes that Germany can be appeased by soft treatment. Moreover, after the beating they have already had, their propagandists are bound to represent any settlement—short of unconditional surrender by the Allies—as iniquitous. It is the opportunity to do ill deeds that must be denied, at any rate until a new generation has grown up.

We are often told that it is no use making arrangements now, however just and however desirable, that will be considered harsh and oppressive by the British people in five years’ time and thrown overboard. The short answer is that it is the first five years that count. When we have re-established our exports and are paying our way, we may be able to afford to be more generous.

It is, of course, difficult to forecast the moods of the public five years ahead, but of one thing we can be certain: if they are then suffering from poverty and unemployment, they will find it very difficult to understand why this Government, at the end of a war in which so much had been sacrificed, deliberately helped to build up German competition in the export markets.

Finally, the moral issue is perfectly clear. The vast foreign debts we have incurred, the loss of our overseas assets, of much of our shipping and of many of our pre-war markets, in fact all the sombre aspects of our painful economic situation, are the direct result of German aggression. Britain must expand her exports or starve. Germany can live without. Everyone agrees that she should face sacrifices in order to repair the damage she has done to other countries. Who then can condemn Britain if she seeks restitution in the German export markets?

VI. — Conclusions.

My conclusions are as follows:

1. It is far more important to this country to re-establish British exports than to obtain German manufactured goods as reparations.

2. For this reason alone, we should discourage the restoration of German industry. But quite apart from this, such a policy would give far greater military security than any other scheme likely to be devised.

3. The instructions to our representatives on the Reparations Commission should therefore be to try to confine reparations to existing equipment, raw materials and, if the Russians insist, indentured labour.

4. Meanwhile British representatives on the Combined Civil Affairs Committee should be instructed to stop any efforts to rebuild German industry, especially heavy industry, whatever the reason, until the whole question has been settled with our principal allies.

C.

Great George Street, S.W. 1,
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