FEDERAL RESERVE BULLETIN

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INTERNATIONAL FLOW OF GOLD AND DOLLARS, 1951

The movement of gold between the United States and the rest of the world was reversed during 1951. The outflow from the United States, which began with the devaluations of 1949 and increased sharply after the outbreak of the Korean conflict, came to an end in the first half of the year. In the second half, gold began to flow back into the United States, whose gold stock was at approximately the same level at the end of December as a year earlier.

Total foreign dollar holdings fluctuated only moderately during the year. While they were drawn down to some extent for conversion into gold during the latter part of 1950 and the first quarter of 1951, they showed little over-all change in the following months. A modest increase toward the end of the year brought the total to the same level as a year earlier. The arrest in the conversion of dollar balances into gold early in the year reflected in part a strengthening of foreign confidence in the stability of the dollar following the adoption in the United States of monetary and other measures to curb inflationary pressures.

The combined gold and dollar holdings of foreign countries increased by almost a billion dollars in the first half of the year, and decreased by about the same amount in the second half. This reversal was mainly associated with a sharp increase in the United States export surplus of goods and services. Transactions of the United Kingdom dominated changes in monetary reserves throughout the year, and the large gold inflow to the United States in the second half reflected a sharp deterioration in the external position of the sterling area. By the end of the year, this area had lost about half of the gold added to its reserves in the period from the devaluations of 1949 to the spring of 1951. These losses by the sterling area, as well as a decline in gold and dollar holdings by Latin America, were offset by increases in the case of Continental Western Europe, Canada, and Asia.

Changes in the distribution of foreign gold and dollar holdings among individual countries during 1951 reflected divergent inflationary pressures and other factors exerting influence over the movement of goods, services, and capital. Wide shifts in international trade, despite import restrictions and exchange controls, induced governments and international agencies to give renewed attention to domestic fiscal and monetary policies. The monetary authorities in many countries made greater use of general credit measures to restrain the supply and to increase the cost of credit and money. These policies reflected a growing recognition of the need to reconcile with the requirements of defense the objectives of internal and external balance and the maintenance of social and political stability.

United States Export Surplus and Foreign Aid

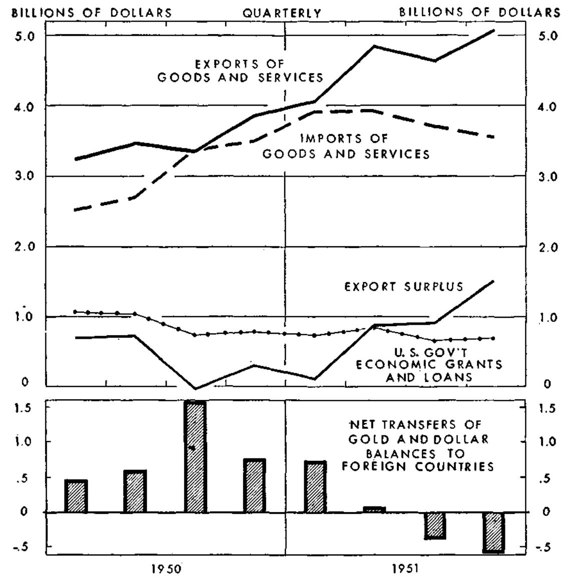
The most significant influence on the overall changes in foreign gold and dollar holdings in 1951 was the sharp increase in the United States export surplus of goods and services. A contributing cause was a moderate contraction of United States foreign economic assistance from the first to the second half of the year.

The export surplus (including services, but excluding shipments and transfers under military aid), which had averaged nearly 500 million dollars a quarter during 1950, was only 150 million in the first quarter of 1951. It then rose to about 900 million in both the second and the third quarter and to 1.5 billion in the last quarter of the year. On the other hand, United States net grants and loans to foreign countries (exclusive of military assistance), which had averaged about 900 million dollars a quarter in 1950 and were still running at more than 800 million a quarter in the first half of 1951, declined to a quarterly rate of around 700 million in the second half of the year.

As a result United States financial assistance exceeded the export surplus throughout 1950 and in the first quarter of 1951, the two figures were nearly in balance in the second quarter of 1951, and the export surplus greatly exceeded foreign aid in the second half of the year, as shown in the chart. The rise in the export surplus and the decline in foreign aid, to the extent that they were not offset by an outflow of private capital and donations, were closely reflected in the movement of foreign gold and dollar holdings, as the lower section of the chart shows.

The virtual balance achieved on current account between the United States and the rest of the world in the second half of 1950

BALANCE OF PAYMENTS OF THE UNITED STATES
SELECTED COMPONENTS



Note.—Net transfers of gold and dollar balances include net foreign purchases of gold from United States plus net increase in foreign dollar balances; Federal Reserve data. Other data from Department of Commerce. Exports of goods and services are net after deduction of military aid. U. S. Government economic grants and loans exclude miscellaneous unilateral transfers and short-term capital.

and the first quarter of 1951 was in part the result of the currency devaluations of 1949 and in part the short-run effect of the Korean conflict. After the first quarter of 1951, prices in the United States showed a tendency to level off. While economic activity in this country remained at a high level for the rest of the year, prices of many imported raw materials declined, leading to a moderate fall in the value of imports from the all-time peak reached in March. Imports of goods and services were at a quarterly rate of 3.6 billion dollars in the third and fourth quarters of 1951, as compared with a rate of nearly 4 billion in the first two quarters. Notwithstanding this decline, imports of goods and services for the year as a whole were at a record level—15.1 billion dollars as compared with 12.1 billion in 1950.

Contrary to widespread expectations of a decline, United States exports of goods and services (excluding military aid) amounted to 18.6 billion dollars in 1951 as compared with 13.9 billion for the preceding year. Rising defense outlays and inflationary pressures in many countries sustained an active demand for American goods which, except in a few lines, continued in plentiful supply, partly because of some contraction of civilian demand in the United States. Nonmilitary exports of goods and services rose from a quarterly rate of about 4 billion dollars in the last quarter of 1950 and first quarter of 1951 to more than 5 billion in the last quarter of 1951.

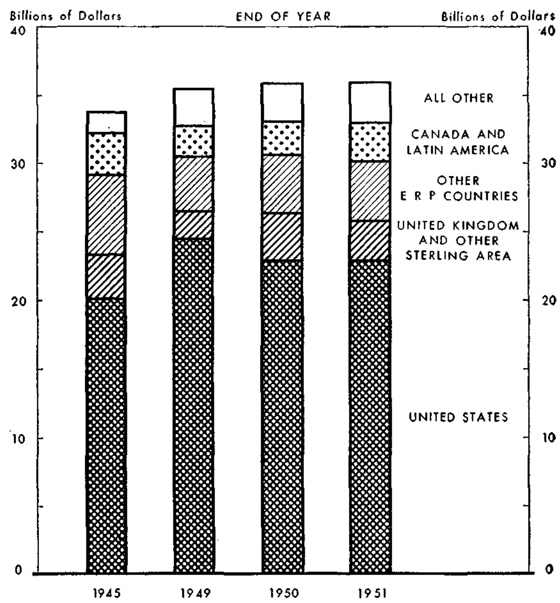
Movements of Gold

Changes in the export surplus and foreign aid of the United States during 1951 were reflected in the movement of gold. The heavy outflow of late 1950 carried over to early 1951, climaxing in record net sales by the United States Treasury to foreign monetary authorities of 880 million dollars of gold in the first three months of the year, as shown in the table on page 230. Before the end of the first quarter, however, the peak had been reached.

Following announcement early in March of more restrictive monetary and debt management policies, the rate of outflow began to decline, and by the end of March had almost ceased. Net weekly sales of gold averaged 83 million dollars in the 10 weeks ending March 7 but only 34 million in the following three weeks. Net sales by the United States Treasury of only 57 million dollars in the second quarter of the year were followed by net purchases of 290 million in the third quarter and 715 million in the final quarter.

The net effect of these changes over the year was a slight increase in the United States gold stock to 22.9 billion dollars as of December 31, 1951. This amount represented almost two-thirds of the world's gold reserves, excluding those of the U.S.S.R., as may be seen in the chart.

WORLD GOLD RESERVES
EXCLUDING U.S.S.R.



Foreign transactions with United States. Of the total sales of gold by the United States in the first quarter, about half was acquired by the United Kingdom; the remainder was divided almost equally between Continental Western European countries (including the Bank for International Settlements) and Latin America. When the movement reversed in the second half of the year, British sales of gold represented nearly the entire amount of United States net purchases, as transactions by other countries tended to offset one another.

The United Kingdom sold much more gold to the United States in the second half than it acquired in the first half, its net sales to this country over the year amounting to nearly half a billion dollars. In addition, South Africa sold a portion of

NET FOREIGN PURCHASES OF GOLD FROM THE UNITED STATES, 1951[1]

[In millions of dollars]

Area and country	Jan.-Mar.	Apr.-June	July-Sept.	Oct.-Dec.	Year
ERP countries (other than United Kingdom):					
Belgium and Belgian Congo	20	−2	......	......	18
France	92	......	......	−72	20
Portugal	10	15	5	5	35
Sweden	15	......	17	......	32
Other ERP countries	39	2	5	4	50
Bank for International Settlements	25	9	−4	......	30
Total	201	24	23	−63	185
Other Continental Europe	......	......	3	−3	......
United Kingdom	400	80	−320	−630	−470
Union of South Africa	......	−13	−20	−19	−52
Canada	......	10	......	......	10
Latin America:					
Argentina	50	......	......	......	50
Colombia	−14	......	−4	......	−18
Cuba	......	......	20	......	20
Mexico	124	−64	......	......	60
Uruguay	51	−15	−28	−30	−22
Other Latin America	26	6	......	4	36
Total	237	−73	−12	−26	126
Asia:					
Indonesia	20	......	......	25	45
Other Asia	2	4	5	1	12
Total	22	4	5	26	57
Egypt	20	25	31	......	76
Grand total	880	57	−290	−715	−68

[1] Minus sign indicates net sale to the United States.

its newly mined gold to the United States. On the other hand, Continental Western European countries purchased almost 200 million dollars of gold from this country over the year, and Latin America and Asia also added to their gold reserves through net purchases from the United States.

Other changes in foreign gold reserves. The gold position of individual countries was also affected by accruals from new production, by sales from reserves for industrial or other private uses, and by transactions among foreign monetary authorities. For example, the United Kingdom, which made net sales of gold of less than 500 million dollars to the United States in 1951, ended the year with an estimated 700 million dollars less in gold reserves than it had at the beginning of the year, as is shown in the table on page 232. This reflects gold transfers to third countries (partly through the European Payments Union) in excess of the gold acquired from sterling area production. Among other countries, Mexico, which bought 60 million dollars of gold from the United States during 1951, showed no increase in its gold reserves for the year.

Canada, a gold-producing country, showed a net increase in its gold reserves over the year of 260 million dollars, almost half representing purchases from countries other than the United States. Nonproducing countries which added more to their gold reserves than can be accounted for by their transactions with the United States include net creditors over the year of the European Payments Union (Italy, Belgium, Portugal, Germany, and Sweden), as well as Cuba and Indonesia. Finally, there were unpublished transactions in the gold holdings of certain Western European countries and the Bank for International Settlements; these are included in "other ERP countries and accounts" in the table on page 232.

Foreign countries as a whole sold about 70 million dollars net in gold to the United States during 1951, transferred another 35 million to the International Monetary Fund, and showed a small increase of 35 million in gold reserves. Foreign gold production (exclusive of the U.S.S.R.) may be estimated at around 760 million dollars for the year. It would thus appear that about 600 million dollars of gold either went into industrial uses or private holdings, or was otherwise unaccounted for. This unexplained residual has been increasing in recent years, the estimated figure for 1950 having been 335 million dollars. It may reflect in part transactions on free and black markets, in which gold is traded privately at premium prices. On the other hand, part of the residual may be explained in other ways as information on undisclosed foreign holdings and transactions becomes available.

Changes in Foreign Dollar Holdings

Dollar holdings of foreign countries, which are held as deposits in Federal Reserve and commercial banks or in United States Government short- or medium-term securities, were about the same at the end of 1951 as at the beginning. There were significant fluctuations, however, from quarter to quarter, from country to country, and as between types of holders.

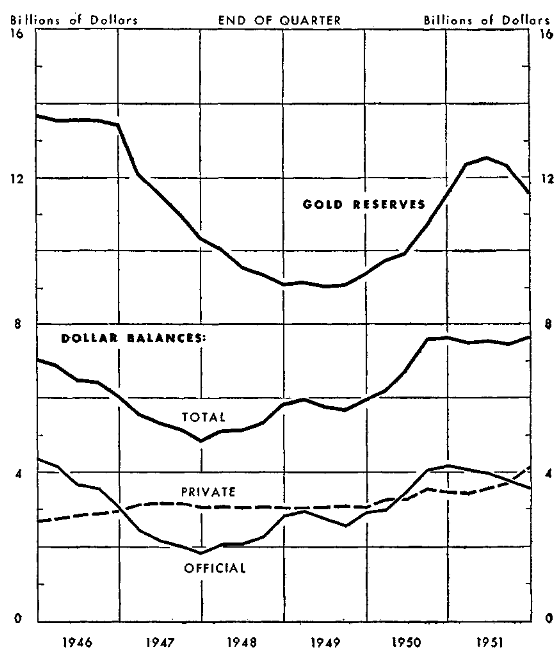
In the first three months of the year, a number of foreign countries drew down their dollar balances to some extent for conversion into gold. Mexico and, to a lesser degree, a few European countries participated in these operations, which came to an end toward the close of the first quarter. In the second quarter, foreign dollar holdings showed no significant changes. After midyear, as the over-all position of certain foreign countries weakened, a net decline of 70 million in their dollar holdings accompanied the larger foreign losses of gold of the third quarter. In the last three months of the year, a number of countries experienced some recovery, leading to an over-all rise in foreign dollar holdings of 165 million dollars for the quarter.

While these changes tended to offset one another over the year, individual countries and areas showed diverging movements. The dollar holdings of Continental European countries as a group rose somewhat during 1951 as a result of an increase of 185 million dollars by Germany, partly offset by declines in the case of other countries. Holdings by Latin American countries and by Canada declined over the year, while those of Asiatic countries increased.

Analysis of dollar movements by type of holder reveals that the absence of net change in the aggregate amount over the year was the result of a decline in official balances—that is, those held by foreign central banks and governments—offset by an equal rise in private foreign balances held by banks, businesses, and individuals. This offsetting movement was in the neighborhood of 600 million dollars. If reported private dollar balances are adjusted to exclude Japanese holdings (which are technically reported as private, though in reality of an official character), the shift becomes smaller, but is still considerable.

The movement in private balances in 1951 was larger than in any other postwar year, as shown in the chart. It was partly the result of the heavy movement of investment capital to Canada throughout the year. Speculation against the pound sterling and the French franc in the summer and autumn probably contributed to the accumulation of dollar balances in private foreign accounts.

FOREIGN GOLD RESERVES AND DOLLAR BALANCES



INTERNATIONAL FLOW OF GOLD AND DOLLARS, 1951

ESTIMATED CHANGES IN FOREIGN GOLD RESERVES AND DOLLAR HOLDINGS DURING 1951[1]

[In millions of dollars]

Area and country	Holdings at end of 1950		Increase or decrease (—), 1951										Holdings at end of 1951p	
			Jan.-Mar.		Apr.-June		July-Sept.		Oct.-Dec.p		Year—1951p			
	Gold reserves	*Dollar holdings*	Gold reserves	*Dollar holdings*	Gold reserves	*Dollar holdings*	Gold reserves	*Dollar holdings*	Gold reserves	*Dollar holdings*	Gold reserves	*Dollar holdings*	Gold reserves	*Dollar holdings*
ERP countries (other than United Kingdom):														
Belgium-Luxembourg (and Belgian Congo)	650	*198*	47	*−16*	−44	*8*	59	*4*	−16	*6*	46	*3*	696	*201*
France (and dependencies)	[2] 543	*291*	......	*−8*	25	*27*	......	*−57*	......	*77*	25	*39*	[2] 568	*331*
Germany (Federal Republic of)	......	*222*	......	*21*	......	*115*	......	*145*	28	*−97*	28	*184*	28	*406*
Italy	[3] 258	*315*	......	*−8*	......	*−30*	24	*12*	53	*13*	77	*−14*	[3] 335	*300*
Netherlands (and Netherlands West Indies and Surinam)	335	*224*	......	*6*	......	*−70*	......	*6*	5	*18*	5	*−40*	340	*184*
Portugal (and dependencies)	207	*50*	10	*7*	15	*−7*	17	*2*	30	*−4*	72	*−2*	279	*48*
Sweden	90	*115*	24	*−10*	15	*−6*	−1	*−10*	24	*−19*	62	*−45*	152	*71*
Switzerland	1,470	*553*	−22	*−48*	3	*4*	−5	*2*	6	*10*	−18	*−32*	1,452	*521*
Other ERP countries and accounts[4]	723	*387*	41	*−29*	−2	*−29*	29	*30*	−144	*−4*	−76	*−33*	647	*354*
Total	4,276	*2,355*	100	*−85*	12	*12*	123	*134*	−14	......	221	*60*	4,497	*2,416*
Other Continental Europe[5]	475	*97*	−20	*−13*	6	*4*	......	*−4*	1	*−1*	−13	*−14*	462	*83*
Sterling area:														
United Kingdom	[6] 2,900	*657*	475	*−18*	150	*−19*	−425	*−107*	−900	*129*	−700	*−15*	[6] 2,200	*642*
U. K. dependencies	......	*120*	......	*−21*	......	*−4*	......	*−2*	......	*3*	......	*−23*	......	*97*
Union of South Africa	197	*44*	8	*−23*	5	*−4*	......	*−5*	−20	*−5*	−7	*−37*	190	*7*
Other sterling area[7]	406	*97*	6	*13*	9	*19*	8	*−15*	7	*47*	30	*63*	436	*161*
Total	3,503	*918*	489	*−49*	164	*−8*	−417	*−129*	−913	*174*	−677	*−11*	2,826	*907*
Canada	590	*1,398*	28	*−70*	34	*2*	39	*−87*	159	*61*	260	*−94*	850	*1,304*
Latin America:														
Argentina	216	*302*	72	*43*	......	*−2*	−12	*−32*	−8	*−62*	52	*−52*	268	*250*
Brazil	317	*226*	......	*34*	......	*−47*	......	*−72*	......	*−41*	......	*−126*	317	*100*
Cuba	271	*259*	......	*17*	10	*52*	30	*−16*	......	*−61*	40	*−7*	311	*252*
Mexico	208	*207*	96	*−98*	−76	*15*	−37	*20*	17	*14*	......	*−49*	208	*158*
Uruguay	236	*75*	59	*7*	−15	*−7*	−28	*5*	−31	*5*	−15	*10*	221	*85*
Venezuela	373	*85*	......	*5*	......	*−14*	......	*1*	......	*−4*	......	*−13*	373	*72*
Other Latin America	249	*431*	14	*25*	−14	*24*	24	*−52*	−16	*44*	8	*40*	257	*470*
Total	1,870	*1,585*	241	*33*	−95	*21*	−23	*−146*	−38	*−105*	85	*−198*	1,955	*1,387*
Asia:														
Indonesia	208	*115*	20	*23*	1	*13*	......	*27*	50	*−37*	71	*26*	279	*141*
Japan	128	*459*	......	*−52*	......	*−64*	......	*150*	......	*104*	......	*137*	128	*596*
Philippine Republic	3	*374*	1	*21*	1	*9*	1	*−34*	1	*−40*	4	*−45*	7	*330*
Other Asia	356	*226*	1	*54*	3	*34*	1	*2*	2	*1*	7	*93*	363	*318*
Total	695	*1,174*	22	*46*	5	*−8*	2	*145*	53	*28*	82	*211*	777	*1,385*
All other countries	101	*100*	20	*16*	27	*5*	31	*19*	−1	*9*	77	*50*	178	*150*
Grand total	11,510	*7,627*	880	*−122*	153	*28*	−245	*−68*	−753	*166*	35	*4*	11,545	*7,631*

p Preliminary.

[1] Dollar holdings represent official and private balances reported by banks in the United States and include holdings of U. S. Government securities with original maturities of up to 20 months.

[2] Represents gold reserves of Bank of France and French dependencies only.

[3] Represents gold reserves of Bank of Italy ($222 million) plus gold earmarked for special purposes.

[4] Includes holdings of Bank for International Settlements (both for its own and European Payments Union account), gold to be distributed by the Tripartite Commission for Restitution of Monetary Gold, and unpublished gold reserves of ERP countries.

[5] Excludes gold reserves of, but includes dollar balances held by, the U.S.S.R.

[6] Estimated gold holdings of British Exchange Equalization Account, based on holdings of gold, U. S. and Canadian dollars as reported by British Government.

[7] Excludes Eire and Iceland, which are included under "Other ERP countries and accounts."

The decline in official balances in 1951 was partly reflected in the withdrawal of 370 million dollars from foreign deposits held with Federal Reserve Banks, but in addition there was some sale by foreign monetary authorities of United States Government securities. Net additions to private dollar balances were in large part held in deposits with commercial banks, but to some extent were invested in United States Government securities.

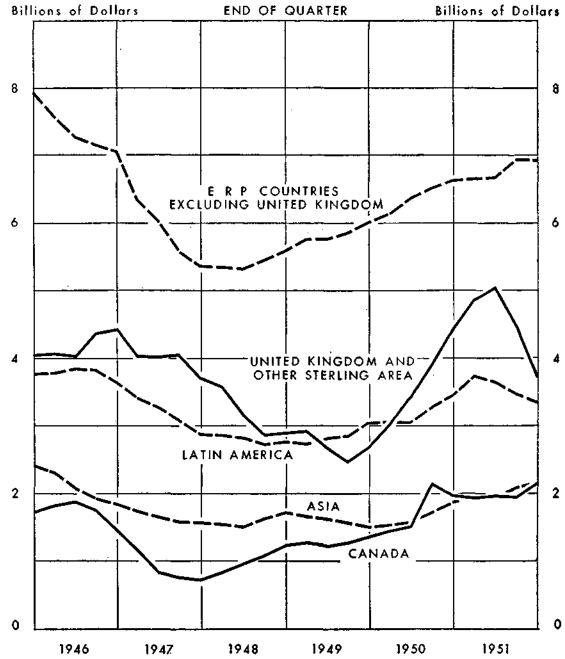
Reserve Positions of Foreign Countries

The combined gold reserves and dollar holdings of foreign countries showed a net increase in the first half of the year of 939 million dollars (heavily concentrated in the first quarter), which was followed by a net decline in the second half of 901 million, as shown in the table on page 232. Total holdings at the end of the year stood at an estimated 19.2 billion dollars, a little higher than at the beginning of the year.

The United Kingdom, which holds the central monetary reserves of the sterling area, accounted for the greater part of the movement of gold and dollars during 1951. Part of the reversal for the sterling area shown on the chart was the result of an adverse trade balance with Canada, Latin America, and Continental Western Europe, and part was the result of capital movements. In considerable measure, also, the changes in sterling area reserves were accounted for by a marked shift in the trade balance with the United States. As exports from this country to the sterling area increased, and imports declined, the United States trade balance with that area changed from a 350 million dollar import surplus in the first half of 1951 to an export surplus of 440 million in the latter half of the year. Coinciding with this adverse shift in the trade balance was a contraction of disbursements by the Economic Cooperation Administration to the United Kingdom and other sterling area countries from about 270 million dollars in the second half of 1950 to 150 million in the first half of 1951 and 100 million in the second half.

Continental Western Europe increased its reserves during the year by about 280 million dollars; the aggregate dollar deficit of this area continued to be more than offset by financial assistance from the United

FOREIGN GOLD RESERVES AND DOLLAR BALANCES
SELECTED COUNTRIES AND AREAS



States. Gold and dollar movements among Western European countries were mainly determined by their transactions through the European Payments Union. This institution, established in 1950, provides for the clearing of intra-European payments and for fractional settlement each month in gold or dollars of the net deficits and surpluses of member countries with the Union. Over the year 1951, Belgium, Germany, and Italy received the largest sums of gold and dollars from EPU, in the net amounts of 229 million, 132 million, and 93 million dollars, respectively. The United Kingdom, on behalf of the entire sterling area, made the largest net payments to EPU over the year, amounting to 110 million dollars, while France paid 42 million. There was a shift from the first to the second half, however; in the first six months the United Kingdom, Belgium, and Switzerland were the largest gold and dollar recipients, mainly at the expense of the Netherlands and Austria. In the second half, the position of the United Kingdom and France deteriorated seriously, and they made the largest payments to the Union. The largest recipients of gold and dollars in this period were Belgium, Germany, and Italy.

Latin American gold and dollar holdings, which had risen in the first quarter of 1951 when wool and coffee sales were seasonally high, declined in each succeeding quarter, mainly because of a shift in the trade balance with the United States, and ended the year with a net loss of 113 million dollars. Exports from this country to Latin America were substantially larger in the second half of the year than in the first, whereas imports remained somewhat low until the end of the year. These trends were particularly noticeable in the case of Brazil, whose imports from the United States increased sharply from the 1950 level while its exports tended to decline.

Although Canada had a large import surplus with the United States in 1951, it was more than offset for the year as a whole by the combination of an export surplus with other countries, a capital inflow from the United States, and domestic gold production. The current-account deficit with the United States outweighed the favorable balance-of-payments factors in the first and third quarters, leading to reserve losses, while gains in the other quarters, particularly the fourth, resulted in a substantial increase in reserves for the year.

Asiatic countries as a group (excluding members of the sterling area) added to their reserves steadily over the year, except in the second quarter; the over-all increase amounted to about 300 million dollars. Japan's dollar holdings fell in the first half of the year, but more than recovered in the second half, with a net increase of 140 million for the year as a whole. Indonesia's acquisition of gold and dollars accounted for most of the remainder. Procurement of goods and services for United Nations forces in Korea and expansion of commercial exports were mainly responsible for the rise in Japan's reserves, while Indonesian increases were largely attributable to increased exports of strategic raw materials and to restrictive import policies.

Situation in the United States and Movements of Gold

Foreign countries normally maintain a substantial portion of their reserves in gold. After the great depletion of foreign gold reserves during and following the war, it was to be expected that foreign countries would convert part of any net accruals of dollars into gold. This is what occurred during the year following the currency devaluations of September 1949. Foreign reserves, both of gold and of dollars, rose each successive quarter beginning with the final quarter of 1949. However, in the last part of 1950 and the early part of 1951 an increasing number of countries chose to add to their gold holdings rather than to their dollar balances and in certain cases actually drew down their dollar balances to purchase gold.

This growing preference for holding gold rather than dollars was an unusual development which largely reflected uneasiness abroad over inflationary tendencies in the United States and their possible future impact on the dollar. After the outbreak of the Korean conflict, prices in the United States advanced sharply and by the first quarter of 1951 the wholesale price level was 20 per cent higher than in the corresponding quarter of 1950. This price advance preceded rises in many other countries. Foreign monetary authorities, on the basis of past experience with inflation in their own countries and in view of international political conditions, became more cautious about holding their reserves in the form of dollar balances and increased the proportion held in the form of gold. In the atmosphere then prevailing, emphasis was placed on short-run factors and less consideration was given to such basic facts as the productive capacity of the American economy, the very large gold stock of the United States, and the readiness of the United States Treasury to convert dollars into gold at the established price to meet any monetary and other legitimate requirements of foreign governments and central banks.

Such tendencies changed sharply early in 1951. Foreign dollar holdings stopped declining in the second quarter, and during the latter part of the year private dollar holdings increased. Official holdings of dollars, as well as of gold, declined because of the growing trade deficit with the United States. The most important immediate factor accounting for the cessation in the conversion of foreign dollar holdings into gold appears to have been a marked change in foreign expectations relating to inflationary prospects in the United States.

The rise in the wholesale price level in the United States ceased early in 1951, and prices remained fairly stable during the remainder of the year. Among the factors bringing about this change were the introduction of wage and price controls late in January 1951; an unexpectedly high level of civilian output; a reduction in the rate of consumer purchases following the wave of scare buying in anticipation of shortages and rising prices; and some reduction in international tension. In addition, there was the adoption of monetary and debt-management policies designed to minimize further monetization of United States Government securities through Federal Reserve purchases. This action in particular assured foreign monetary authorities that the United States was determined to take adequate steps to maintain the stability of its currency, and thereby largely removed the main motive to maintain a greater than normal portion of their reserves in the form of gold.

Foreign sales of gold to the United States and the accompanying decline in foreign official deposits at the Federal Reserve Banks in the second half of 1951 had a direct effect on the monetary situation in the United States. The inflow of gold in this period was equal to the net addition of 1.0 billion dollars to member bank reserves; the effects of other relevant factors on such reserves tended to be offsetting. The inflow of gold was the most persistent element adding to bank reserves in these months, and permitted further growth of bank credit and expansion of the privately held money supply.

International Reserves and Monetary Policies

Events during 1951 provided ample illustration of the close connection between internal financial policies and the balance of payments. Countries in which inflationary pressures were unabated or growing, such as Austria, France, the United Kingdom, and Brazil, were faced with a sharp deterioration in their external positions. This situation led the United Kingdom late in 1951 and in March 1952 to adopt restrictive fiscal and monetary measures, accompanied by a planned curtailment of imports. Countries such as Belgium, Italy, and Portugal, which continued to rely on general measures of restraint over the supply of money and credit, succeeded in maintaining or improving their external balance. Germany, which in the latter part of 1950 had suffered a rapid deterioration in its balance of payments, was able in 1951 to reverse its position by internal credit measures, supported by temporary trade controls which were abandoned as the situation stabilized.

Increased awareness of the importance of budgetary restraint and monetary stability led to greater use of anti-inflationary fiscal and central banking measures. There was renewed emphasis on the traditional tools of monetary policy, including use of the discount rate. Cheap-money policies, which had been favored on various grounds during the early postwar years, were looked upon with increasing misgiving, and there was a growing reluctance to freeze interest rates at levels which could be maintained only by inflationary expansion of the supply of money and credit. The need for strong internal financial policies was increasingly felt as the defense efforts of many countries added to inflationary pressure.

The weakening in the external position of countries experiencing inflationary pressures occurred in spite of the widespread use of direct restrictions on trade and payments. Postwar experience indicates that such measures have serious shortcomings for the purpose of eliminating or reducing fluctuations or swings in the balance of payments. Such swings have continued to occur in recent years and, in some degree, restrictions have actually shown a tendency to intensify or prolong them. Short of direct interference with transactions in process, the full effectiveness of trade restrictions is felt only after an interval of weeks or months, and restrictions adopted to meet a particular situation may prove inappropriate to meet the situation prevailing at the time they become effective. Moreover, when the external position of a country appears to be deteriorating, the threat of new restrictions tends to stimulate the demand for imports, thereby placing the control mechanism under increased pressure and frequently leading to anticipatory imports. Under such conditions the restrictions adopted may be more severe than the longer run situation requires.

Exchange restrictions also tend to eliminate equilibrating movements of short-term capital and to impair the flow of long-term investment capital, and at the same time they have often proved inadequate to deal with speculative movements of funds. It appears, for instance, that in 1951 expectations of changes in exchange rates induced substantial speculative movements of short-term funds, effected largely by anticipating or delaying settlement of trade transactions.

The reversal in international payments of certain countries in 1951, notwithstanding trade and payment restrictions, has given rise to a new concern with respect to the adequacy of monetary reserves. Since fiscal and monetary measures require time to take full effect, reserves of gold and convertible currencies have again emerged as essential instruments to cushion temporary difficulties and to facilitate longer run readjustments. Recent events have dimmed the hope, which had arisen from the devaluations of 1949, that foreign countries would be able, in a comparatively short time, to build their reserves to a level regarded as adequate to meet possible swings in international payments. On the other hand, the same events have deepened the conviction that there are no easy alternatives to positive fiscal and monetary measures if countries are to meet the requirements of defense while maintaining internal and external stability.