Chapter VI

AIMS OF A REGULATION OF INTERNATIONAL ECONOMIC RELATIONS

In the preceding five chapters we have endeavoured to make clear the essence of international economic relations. We will now, in the five chapters following, deal with the question whether, and if so, how a certain regulation of these relations should be aimed at. In doing so, we will take existing conditions as our starting-point; not the conditions of wartime, but those which will, after a certain period of transition, develop into a more normal situation. Hence we do not mean to deal with those temporary measures which will prove to be necessary in order to alleviate the greatest distress or in connection with military operations; it is the more final arrangements that will form our subject-matter.

If the conditions that prevailed in the international economic field between 1918 and 1939 are reviewed, the conclusion is evident: the chaotic development of those years can in many respects not be put up with again. It was far too much incidentally that the difficulties arising after the First Great War were faced; a policy of tinkering and makeshift. Therefore, in view of the presumably far greater difficulties which will arise after the Second World War, recourse should a fortiori be had to a programme that has been well thought out and for whose execution people are ready to use force. A programme presupposes an aim; it is this aim about which we will speak in this chapter. It is not difficult to find a formula for it, which as a formula will satisfy anybody: as our aim we wish to put the

promotion of 'general interest'. It is more difficult, however, to make this formula more concrete. We already wrote about these difficulties elsewhere[1], therefore we shall here only give a summary of the conclusions reached there. These were, for instance:

1. The idea of 'general interest' must remain vague as long as no method has been found to weigh a decline in the satisfaction of one person's wants against an advance in those of another.

2. The satisfaction of anybody's wants is dependent on greatly varying aspects of human life: the possession of material goods, health, a certain measure of liberty, opportunities of employment and a certain measure of certainty in life; promotion of one aspect often causes a neglect or opposition of the other.

3. People often do not know their own happiness: they have incorrect or too limited conceptions about it.

4. People differ greatly in natural ability, accomplishments and desires: tastes and requirements differ.

Viewed internationally this becomes even more difficult, because between the various nations, too, there are great differences in their views of life, ability, wealth and history, which appear, for example, from their widely different aspirations and forms of government (compare Germany, Japan and Russia with the western nations on the one hand and the oriental countries on the other); and in the sovereign power of nations, hitherto accepted, in many matters which also touch their neighbours and other countries in the world.

These difficulties may result in a permanent difference of opinion as to the aims of economic policy and are the cause that any programme will show subjective elements

[1] De les van dertig jaar, chapter 12.

as long as these difficulties have not been solved. For instance, certain suppositions have to be made about the relative importance of the desires of one man compared with those of another, and one must presume to give an opinion on what is good for others, even if they do not see it themselves.

The complete solution of the problem of the organization of the international community, however, is not the task of the economist. The latter has only to occupy a discreet place beside the expert on matters of government, other experts of organization, the psychologist and the pedagogue, the sociologist and many technical experts. As for the problems touching himself, he will have to be on his guard against inexpert solutions; in the past he has been listened to far too little: witness what happened to Keynes after 1919; but it should not be thought either that everything will come in order once the economic problems have been solved. Even more than after 1918, much has been destroyed this time that belongs to the competency of others. Moreover, new branches of science have since revealed to us aspects of the community which must on no account be neglected. One group of surgeons, at any rate, will have to be more modest than in 1919: the politicians. For the very good, real politicians this holds good to a lesser degree than for those among them who, properly speaking, are nothing but representatives of group-interests. It is to be hoped that especially the solution of the most difficult problem, the finding of the correct treatment of the conquered peoples, will not be left to the feelings of politicians only, but will also be based on the opinions of a great number of sociologically-schooled scientific men.

In this publication only the economic aspect will be elucidated to some extent. In our opinion, the aims of a

regulation of international relations may, in this respect, be formulated as follows, according to the further investigations mentioned above:

(a) a production as large as is possible;
(b) a production of the greatest possible stability;
(c) a distribution, as fair as is possible, among
1. persons and classes, and 2. peoples;
(d) a number of conflicts as low as possible, both within the borders of each country separately and among the various nations;
(e) a liberty as great as is possible for the parts, i.e. for individuals, enterprises and states.

It should be borne in mind, however, that these aims are not entirely independent of each other and that it is possible, therefore, that the promotion of one of these aims is prejudicial to another. Hence the question remains to be answered how these aims, as far as they are in conflict with each other, are to be weighed one against the other. As long as measurements are still impossible in this respect, it will be necessary, as was pointed out in another connection, to leave this weighing-off largely to the subjective judgment of the economic-politician. The aims under (d) and (e) have a more passive meaning: especially with regard to the question of liberty it should first be investigated, in how far the other aims leave the possibility of a certain freedom of the parts. Opposite the possibility of conflicts among the various aims there is the fact that the attainment of one object also brings the other object nearer. Thus the number of conflicts will already diminish, when production has increased and reached greater stability and distribution has become more equitable than before.

Most of these aims have an internal aspect for each

country separately as well as an international aspect; the present work only deals with the latter. This means, as we shall see, that for some points, especially point (a) but also (b) and (c) even the main points will not receive treatment here.

The principal measures by which the aims, mentioned as desirable, can be attained, are, as regards the points (a) and (b), included in a good trade cycle policy in the widest sense of the word. The aim of this policy might be defined as the 'living within one's means' for the entire social system, and then in this sense that — apart from the normal increase of the circulation of money over longer periods — not only not more than the income is spent, but also and especially not less than the income. For the non-spending of the income brings about the depression. 'Spending' in this connection is also using the money for the expansion of plant. After a detailed analysis of the mechanism of economic movements and of the experiences gained with different measures in the field of economic policy, especially since 1929, I have elsewhere[1] come to the conclusion that it is possible to attain a practically full employment of the productive apparatus without the disturbing effects of serious depressions if certain conditions have been fulfilled. The measures necessary for the attainment of this objective are not so far-reaching that every gesture of private entrepreneurs is to be restrained, as in a situation of war-economy or as is the case in Russia. Apart from some exceptional situations which will be dealt with later, it suffices that the authorities should follow a

[1] Economische Bewegingsleer, especially the supplement about „Beïnvloeding der economische bewegingen", Noordholl. Uitgeversmij, Amsterdam 1942-1945.

policy of 'compensatory expenditures'. This policy means that in times of a depression in private business-life a greater number of government orders is given than in times of great activity in the private sector. For this purpose the government must have a reserve of unexecuted public works, of which the preliminary work has been completed already and from which they can draw 'at call'. Also other than only public works can be used, as for instance the ordinary official activities, and the many cultural and social objects by which social life can be raised to a higher level. We are thinking of research-work, the creation of possibilities for travelling and recreation for those big groups of the population whose income is insufficient for these things and many other projects of the kind.

The execution of these projects should not be financed from increased taxation. It is better not to raise the rates of taxation in times of depression, — perhaps even better to reduce them, — because an increase would check enterprise still further. The financing should be done by means of loans and by the creation of new credit, as long as there is no cyclic reserve to draw from. The creation of the latter should be aimed at in boom periods, when the revenues ought to exceed the expenditure of the government. In boom periods it is not desirable to redeem on a larger scale, because in this way large sums would come in the hands of individuals, which might lead too much to new investments. The reserves made in boom periods should not be invested in the ordinary way, but kept liquid, for example as a special account with the Central Bank. For also an investment in securities would mean that money would come at the disposal of the public, which at that moment had better remain inactive.

It is probable that the raising of loans in slump periods

does not attract all the parts of the incomes that have remained unspent. As, however, the aim of cyclic policy in slump periods must be to let the incomes flow on, and thus maintain the level of an approximately full employment, it will be possible by the creation of more new money than is compatible with the structural growth of the social system, to provide a certain compensation. During the slump itself this will not involve any dangers. It will, however, when the recovery announces itself and the amounts hoarded before come into activity, together with the newly created means. If the recovery should develop too rapidly, an economic overstrain might be the result, with wrong investments and a repercussion in its wake. This is the moment when the government may have to intervene to a larger degree than will be necessary in other cases. The means at their disposal are: rationing of credit, of imported raw materials and machinery, perhaps even of raw materials and machinery produced in the country itself, and price-control. When, however, the depression has been mitigated by the measures described above, the revival is also less impetuous than was sometimes the case formerly. For the arrears in replacements, in stocks and in the requirements of consumers are less and only a very small rise in prices will take place, owing to which speculative purchases of raw materials will also be less intensive. Therefore the hope is justified that the circumstances indicated above as exceptional situations, will only seldom occur and that these more drastic measures rather have a preventive character.

The trade cycle policy here drawn in outline — and for the details of which we again refer to the publications mentioned — is, as we also observed before, tied to some conditions as to its practicability. The first and most

important condition is that industry in general shows an understanding for the sense of these measures; especially that it is realized that unhampered trade and industry are of themselves unable to prevent economic fluctuations and that it is therefore a natural duty of the government to see to it. In the U.S.A., between 1933 and 1938, this was insufficiently realized and the high government expenditure led to a strong aloofness in the expenditure of private people, both as regards investments and articles of consumption. This aloofness had a strong adverse influence on industrial activity. If these views should not be reconsidered, the possibilities to attain a reasonable measure of employment and stability in an industrial life that is still free in many other respects, are so slight that the only solution lies in a far more drastic interference of the government: in a sort of war-economy or socialisation on a large scale. Thus, however, initiatives of great value to the community would presumably also be lost, and it is to be hoped, therefore, that industrialists and authorities will appreciate each other's contribution towards the establishment of more stable and better economic conditions and will act accordingly. As far as the industrialists in the Netherlands are concerned, and as it seems equally in Great Britain, I think I am entitled to state that a distinct change in opinions has taken place which gives rise to a feeling of optimism.

A second condition for the success of the economic policy outlined above is that internationally there should arise sufficient cooperation in this respect, so that the national trade cycle policies of the big countries approximately run parallel. If Great Britain should endeavour to follow such a policy — and government utterances give rise to hope in this respect — it must not be thwarted by the

U.S.A., Russia, France or Germany. If these four big powers should work in approximately the same direction, the chance of success for each country separately would be greatly increased, without the necessity of an intricate international system of cooperation. It is to be hoped that especially the U.S.A. will realize their great responsibility in this respect. If there, as is feared by Myrdal, and notwithstanding the warnings of prominent economists such as Hansen and Stuart Chase, economic control should be insufficient in consequence of the attitude of powerful groups of employers, things may be spoilt for the world as a whole.

The measures which in my opinion will especially be necessary to attain the more equable distribution among the persons and classes of one nation as mentioned before under (c), belong to the domain of taxation and social legislation. Proposals in this connection have also been published elsewhere[1]. I am especially of opinion that wage policy offers only limited opportunities, and that large-scale socialisation has by-effects which do not or not yet make it attractive in the present epoch. A common characteristic of importance in the measures of economic policy suggested so far is, that they are chiefly problems which must be solved within the different countries. It is first and foremost of importance to the rest of the world what the big powers, the U.S.A., Great Britain and Russia will do in this respect. International relations are only of secondary importance in this connection, although they must answer certain requirements to which we shall revert later.

By their nature the aims mentioned under (c2), (d) and (e) are, however, to a larger degree questions of international

[1] Redelijke inkomens, 1945.

relations. Thus in chapter IX we hope to expound that a reduction of the differences in the standards of life can mainly be effected by capital export from wealthy to poor countries. A diminution of the number of international conflicts, as far as they are of an economic nature, should be aimed at — besides in the field just mentioned — by banishing arbitrary actions in the domain of commercial policy and technique of payment, tolerated in consequence of the complete sovereign power of nations. We shall revert to these matters in the chapters VIII and X.

The demands which the points (a) and (b) — mainly referring to the internal economic policy of the big countries — make upon international relations, find their origin in the disturbing influences, both on the absolute height and on the stability of production, emanating from international commercial and financial policy. Besides the stability of production in the big countries, they endangered to a much greater extent the stability of production in the small ones. For the small countries are dependent on foreign outlets for such a substantial part of their production that a slump in one of the big countries always brings along difficulties for the small ones. Therefore, the measures of trade cycle policy also have an international aspect for the small countries. Which does not mean to say that a small country should be entirely at the mercy of the waves of the world's economic situation. If it has a sufficient currency-reserve at its disposal, it can greatly mitigate by compensating government measures the consequences for the home market. It will also be able to do something by a suitable rate of exchange policy, if necessary. However, this is not the place to go more thoroughly into these questions, because they have to do with national economic defense rather than international cooperation.

Also for reasons of economic policy, therefore, a limitation of sovereign power is essential; the policy of trade and payments of every country will have to come up to certain requirements. It should be impossible for any one country suddenly to close its frontiers entirely or partly for the products of other countries. Moreover, the financial management should come up to certain demands of stability: great fluctuations in the rates of exchange or even the threat thereof, by inefficient management, should become impossible. A correct settlement of the problem of international war debts and of possible reparation payments will be imperative in this connection. Also these points will be dealt with extensively in the chapters IX and X.

After this brief survey of the principal measures of economic policy which we consider essential for the attainment of the aims mentioned, we shall now treat in detail of those among them which are of especial importance for international relations. The same division of subject matter will be followed as in the First Part of this book. So, before dealing with commercial policy, capital export and financial intercourse in the chapters VIII, IX and X, we will expound in chapter VII what is the significance of problems of population policy for the attainment of a better economic community, and why, for the present, we do not consider transfer of territory a correct means in economic policy. In chapter XI we shall discuss the necessity of an international centre for economic policy, while in chapter XII some observations will be made concerning the position of the Netherlands with regard to international economic cooperation.

CHAPTER VII

PROBLEMS OF TERRITORY AND POPULATION

In this chapter we will for a moment abstract our attention from the concrete military and political situation; especially from the fact that at the present moment the relations between the different nations are still so largely governed by the military aspirations of Germany, Japan and Italy. We will for a moment only consider the economic aspect of these relations, and then in broad outline and for future times; one might say, hoping that all this will one day be possible again. The world's economic problem can then be formulated as follows: in what way can the world's population be given the greatest possible prosperity, divided more equally among the nations?

The prosperity to be attained naturally depends on many diverging factors. Of great importance, as is generally known, are: technical development and the formation of capital; the latter problem will be dealt with more extensively in chapter IX. Of importance are also the possibilities of barter and the manner of distribution, which will likewise be dealt with later. On further consideration, however, one meets with two other factors, of which we shall treat in this chapter.

The first of these factors is that of the *size* and the *growth* of the population. Both exert an influence on prosperity. This influence is rather complicated, but something, at any rate, may be ascertained about it. Let us consider in the first place the influence of the *size* of the population that has so far been reached. In order to do this correctly

and abstract for the present from the influence exerted by the *growth* of the population, let us, in our minds, compare two situations: one of a thinner and one of a denser population. In many respects it is of little importance whether there are many or few of us. Every individual not only has a mouth, but also two hands; speaking in economic terms: he is not only a consumer, but also a producer (though it is true that in the course of his life he is a consumer before becoming a producer; we shall revert to this later on). In some respects a denser population may even be more prosperous: by well-organized cooperation some branches of industry can then work more efficiently. This will hold good especially for traffic, because the living closer together of the population makes mass-transport possible, which is not the case when the population is thinner.

Thus reasoning, we put it for a moment as if in this form of production only labour is required. Actually also capital is necessary. And there things are different. The supply of capital goods at our disposal is partly inherited from the past, and therefore partly independent of the size of the population now. Only the additions to this supply which are made every year, are dependent on the size of the population. Therefore a denser population is at a disadvantage in this respect.

This holds good even more strongly with regard to the soil, hence especially for agricultural and mineral production. The extent of soil and the natural resources contained in it are independent of the size of the population, and the denser the population, the less there is available per head. It is in a country like China that the adverse influence of a dense population appeals most strongly. Four acres per farm is only available there, whereas the most economic size would be 13 acres. The production of

cereals in China is only 1400 kilos per man-year as against 20,000 kilos in the U.S.A.

Also in the Netherlands the problem of land-hunger is known only too well!

A further investigation shows that this influence is of greater importance than the above-mentioned favourable influence of a dense population on the efficiency of some branches of industry such as traffic. Hence it follows that the size of the population has a negative influence on prosperity: the greater the population is, the smaller its prosperity will be, taking it that all other circumstances are equal[1].

We will now look at the influence of the *growth* of the population, i.e. of the fact that at a certain moment the population is increasing. On one hand it is customary to say that a growing population is probably more enterprising than one that, in consequence of a small number of births, is stationary or even decreasing. A growing population, it is said, is a sign of an energetic attitude towards life. This is correct for the person who

[1] Wagemann has brought together statistical material, by which he tries to prove that the relation between density of population and prosperity is indicated by a line alternately falling and rising. He called this the „Alternationsgesetz", which would involve that there is more than one relative maximum and more than one relative minimum in prosperity, and that a country in its development and with an increasing density of population alternately passes through phases of relative overpopulation and relative underpopulation. Germany, Italy and Japan would then find themselves in phases of relative overpopulation. The suggestion is interesting and certainly deserves closer attention. For the present our own investigations make us believe that this alternation is not certain, but that there *is* a broad interval of population densities, inside which the influence of these densities on prosperity is comparatively slight. For the very slight densities, however, the negative influence is quite distinct.

deliberately aims at a large family. But most big families are found among those strata of the population, where it can only partially be said to be a question of deliberate choice. And then the argument of enterprise in such families seems to us to be rather doubtful. It is presumably a matter of quite different forces.

On the other hand the fact of a growing population will probably stimulate production to a certain extent. From the view-point of the separate family, many things are needed in a growing and large family, so they will have to work hard. Considered from the point of view of the social system as a whole, there will be a great demand for new houses and other lasting objects for use and investment in a rapidly growing community. This is of all the more importance, as was already pointed out above, because the new arrivals start their lives with consuming and only begin to supply their productive contributions after a good number of years.

So there is no denying this stimulus for production. But it should not be forgotten that it results from the very fact that, calculated as to the possibilities of consumption per head, prosperity declines in a growing family, i.e. from the fact itself, discussed above, that a large population means a smaller prosperity when all other conditions are the same. And it is highly doubtful whether this stimulus is able to reverse this trend.

On the strength of the above arguments — of which the figures about the influence of the size of the population on agricultural production form the chief part — I do think that also the prosperity of the world's population could grow more rapidly, if the population of a number of countries, such as for example China, India and Japan, but also Holland, should grow less rapidly or even decline.

Apart from this it is equally clear that prosperity would be spread more equally, if the possession of natural resources were spread more equally. Chapter I already dealt with the inequality of this spreading; we saw that it is especially the Anglo-Saxon races that possess a relatively large share of the natural resources.

The two problems that have been broached: that of population and of the spreading of natural resources, are international in character. It cannot leave the rest of the world cold, if at present Italy and Japan, later perhaps China and India, in consequence of over-population have come to the formulation of demands that have as their object the property of races that are blessed with more worldly goods. Even if it should be thought that for example Germany has abused the argument of over-population to mask other intentions with it, this can hardly be maintained in the case of Japan; that country is indeed overpopulated. And once China and India have undergone a further evolution in political respects, it could hardly be resented if the thoughts of these countries should follow the same lines; it can only be hoped that by that time other methods will be followed for putting, considering and meeting such claims. Both nationally and internationally, therefore, the problem of population control is sure to present itself, and sooner or later we shall have to come to an international policy in this connection. By closing one's eyes for it, one fools oneself and perhaps misses opportunities for a happy solution of threatening difficulties, which will no longer be possible once it is too late. Thus the demand put to Japan that this country must withdraw within her 1897 borders, will in point of fact appear to come down to a camouflaged demand of population policy — and a very heavy one at that — in the name of the United Nations.

Unfortunately the discussion about this question is rather heavily weighted with dogmatic conceptions. These are closely related with the moral aspect of birth control, an aspect of which we think by no means lightly. In the penetrating discussion of these problems which, we hope, will start again after some time, all aspects, and certainly the moral one as well, should come up for their share of attention. The only condition which, in our opinion, this discussion should at any rate fulfil is that it be unprejudiced and with appreciation for each other's standpoint. Further it stands to reason that those who have insurmountable objections to birth control should thoroughly realize, what the demand put to Japan actually involves and what will be the logical results of their standpoint for the future level of prosperity.

The problem of the distribution of natural resources is as thorny. On the one hand a certain right of those who have discovered certain territories rich in natural resources, cannot be denied. But this right cannot go very far. Also the consideration that the present possessors of many of the rich territories make a more efficient use of them than possible other possessors, is only a very partial justification of the inequality of the division. It has been tried to parry the call for 'admission to the raw materials' on the part of the 'have-nots' among the countries by the statement that the goods produced in the countries which are rich in raw materials are placed at everybody's disposal at the same price, so that in practice there would be no difference between the possessors and the non-possessors. This argument is very weak, however. For the very production of these raw materials is a source of prosperity, which is desirable in itself and to which every nation has a certain title.

In the long run we cannot imagine a stable world order unless the two great problems mentioned have been given a solution that has more sense than only the maintenance of the status quo.

Just now it would be inopportune to open the discussion about these problems. They are crossed too much as well as obscured at the moment by military and mental aspirations. Japan endeavoured to accompany every economic penetration by setting up power centres. Germany and Italy were driven too much by purely military aspirations, which also on account of the mental forces behind them, were unacceptable to western culture. The resulting wounds must have healed and the basis been found again for actual cooperation in spiritual matters, before the economic problem can come up for discussion, and then unobscured. This will take a long time; let us hope that that time will be used well. At any rate that time may be used to prepare the solution of the two so very difficult problems mentioned. One should not shut one's eyes to them.

Another, more economic aspect of the problem of transfer of territory is touched upon by the recent proposals to add in one form or another part of the German territory to the Netherlands. Some speak of annexation, others of mandated territory; one hears it vindicated that the German population should have to leave that area, whereas others are of opinion that this should not be done. Although this problem does not quite belong to the subject in hand, the temptation to say a few words about it, now that we are in the immediate neighbourhood of it, is too great. We shall restrict ourselves to two aspects of the economic side of the question, though it is evident that the political side is at

least as important[1]. The arguments of the proposers are also largely of an economic nature and are twofold: in the first place they see in such an extension of territory a compensation of the damage to cultivated land which we have suffered in consequence of flooding, in the second place they expect a facilitation of possible reparation payments or achievements. It is pointed out that in this way the transfer problem can be avoided.
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When discussing these arguments discrimination should be made between an extension of territory inclusive of the population now living there and also exclusive. When also the population is transferred to within Dutch borders, the extension only then means an alleviation of our land hunger if the population density in the area to be annexed, calculated per hectare of cultivated soil, is considerably less than with us. We doubt whether valuable areas can be indicated for which this is the case. Should it not be desired to add the population to the Dutch, then they would have to be transferred; it is evident that, even apart from purely humanitarian objections, enormous dislocations would be brought about. Especially in the remaining part of Germany prosperity would be diminished even more strongly, which would cause economic difficulties on a large scale — also for our exports.

[1] Cf., however, appendix III. Moreover, it should not be forgotten that the following text was written already in 1944. Since then, several other aspects have been taken up for discussion.

As to the facilitation of the reparations problem: in a literal sense it is true that no transfer would be necessary; but that is far less important than is generally believed. In chapter V we already pointed out that also for each part of a currency-area — in this case for the annexed German district — payments and receipts must be equal. Reparation payments, also if they could be made in Dutch florins consequently, would still require a strong increase of exports by this territory, for which the same difficulties count as those which are usually — though somewhat unhappily — indicated as transfer difficulties (see also chapter X).

In whichever way it is desired to tackle the reparation problem, either by payments in money or in kind, the difficulty will always remain that then a strong discrimination will have to be applied within our territory: either taxation in the annexed districts will have to be higher or they will be oppressed by supplies in kind. It would seem to us that the existence of such a discrimination within one and the same territory will cause more difficulties than if there should be question of two different countries.

With these arguments the political side of the problem has naturally not received treatment; we shall not enter into the advantages and drawbacks connected with it. However, one should guard against too optimistic a view of the economic effect.

CHAPTER VIII

PROSPECTS AND REGULATION OF INTERNATIONAL TRADE

We shall now start to discuss at closer range the measures in the international economic field that can be and should be taken already now, considering — as announced — in the first place the problems of international commercial policy. We shall preface our observations with some remarks about the prospects of international trade.

In the first few years after the war this trade will certainly not be limited on the part of the requirements: there is a very great need of completion of every imaginable kind of goods-supply in large parts of the world. Although that is not quite the same, it may also be put that on the part of demand — i.e. requirements backed by purchasing power — no limitation will be imposed. In spite of the disposition to economy which will arise on all hands — and may it not go so far that it becomes unwise — we expect the actual demand for goods to be very high, too. The limitation which will be felt at first is more likely to come from the supply. In the countries where the war has raged, much productive capacity will have been lost and it will be some time before countries like Germany, Russia, the Netherlands and so many others will be able to export again. The reconstruction of plant, of livestock, of the stocks of semi-manufactures and raw materials will only gradually proceed, and only after a number of years will the supply of finished goods be comparable again to what it was in 1938. Probably, however, the shipping position will not cause the same concern as in 1919.

Though, consequently, in the period of reconstruction there will be little need for concern about outlets, the problem of exports will, in the opinion of many, emerge again in proportion as the reconstruction gets to the less urgently required goods and more normal conditions begin to prevail again. It is not only in neutral countries and the U.S.A. that all kinds of measures are already being planned and discussed to stimulate exports, i.e. preparations are being made for a new race in competitive measures. Countries reckoning with high obligations for the future — such as, for instance, Great Britain — are not only planning for increased exports, but also for reduced imports. Thus a repetition of the conditions after 1930 is threatening.

This state of mind is typical of the mentality which develops during a slump: every seller is feared for his competitor's supply and efforts are made to keep him out, but it is forgotten that, if he sells more, he can also buy more. This slump mentality is exactly the opposite of what we saw in war time, when competition on the part of demand entirely governed the minds: everybody desired the goods and not the money. Also for the period of reconstruction this latter mentality will have to be taken into account — unless the financial policy should turn out to be too stringent. There is some sense in a slump mentality during a deep depression in so far as there will be a general inclination to spend less than is received. For more normal times, however, such a disposition is, economically speaking, not necessary at all and even to be considered quite harmful.

An example of the exaggerated pessimistic commentaries, caused by a slump mentality, as have been given about the rise of new competitors, is that of Japanese competition after 1929. Because this, particularly for the

gold bloc countries, fell actually in a period of depression, the concern was comprehensible in this case; but the commentaries generally overlooked the fact that Japan in that period not only exported much more, but also imported at least as much more. The following figures will prove this:

IMPORTS AND EXPORTS (WITHOUT GOLD) OF JAPAN, TO COUNTRIES, IN MILLIONS OF YEN:

	Imports		Exports	
	1929	1937	1929	1937
China	210	393	347	395
Kwan-tung	166	45	124	396
India	288	454	198	318
Indonesia	77	153	87	200
Great Britain	153	106	63	168
Germany	157	176	13	43
U.S.A.	654	1270	914	639
Canada	69	105	27	20
Australia	133	165	44	72
Totals (incl. all others)	2216	3783	2149	3175

It is true that Indonesia could not benefit as much by these increased imports as the increased exports from Japan amounted to, at least not directly. In how far it has benefited indirectly by the increased Japanese activity, in consequence of the greater purchasing power of those countries whose export balance to Japan increased, can only be ascertained after further investigation. Moreover, it is quite possible that our sticking to the gold value of the Dutch florin has also tricked us. Last of all it is possible that the goods required by Japan, were not produced by us. Also in its later development Japan will especially need raw materials — for labour it has in abundance —; so

anyone who also wishes to profit by the industrial development of that country — and of other countries — will be wise to offer the raw materials required for it.

Besides the reasons already stated, why — incorrectly, we think — too pessimistic commentaries have been connected with Japanese competition, there is another fact: Japanese expansion was forced in so far that it was based on an inflation which that country will be unable to maintain. This inflation led to prices and wages in money still appearing acceptable to employers and workmen, but the actual remuneration embodied in them, dwindled further and further. Once the adaptation of the cost factors to the increased prices will be complete, part of the industry will be unable to sell any longer at these prices. The real rate of wages fell from 1932 to 1938 by 26 %; export prices, expressed in yen, rose it is true by 36 %, but wholesale prices in general by 56 %. Hence it becomes clear that in this case we had partly to do with an economic development, caused in the first place by the armament inflation, that could not last.

A different mentality from the slump mentality referred to above will be needed for the regulation of international trade, if we are not to fall again into the same restrictions of economic intercourse, which after 1930 caused so much harm and which ultimately were to lead to ruin. Indeed, this does not only hold good for foreign trade; it is a general rule. If it should become fashionable to spend less than one receives, consequently always to adopt a waiting attitude, a renewed stagnation in the economic circulation process will surely result and society cannot suffer this. If free industry, assisted by additional state expenditure in slump years, does not itself see to the necessary expansion and by this maintains employment, only a socialized production can

yield us full employment. Socialization in the present epoch would, however, be attended by all kinds of losses of freedom and initiative, owing to which, in our opinion, this would not benefit society as a whole. If this is correct, it is to be hoped that free industry will have sufficient energy to tackle enough new projects, even if the chances of profit should be somewhat less than formerly in periods of improving economic conditions. For these smaller chances of profit are, in a society with a more stable economic development, offset by a greater certainty, owing to which the risk premium can also be lower. It is further to be hoped that industry will have sufficient understanding for government initiatives meant to extend production; for, as we explained elsewhere, these initiatives are perfectly logical and indispensable in a good economic policy.

A regulation of international trade relations should further be based on the following considerations. In the first place it may be taken that, much more so than between 1919 and 1939, it will prove to be possible approximately to reach a condition of full employment, in consequence of which the slump mentality referred to above is unnecessary. In the second place it must be borne in mind that under such circumstances — according to what we expounded in chapter II — not only no great objections can be raised against free trade, but that the latter will even lead to a higher prosperity than any system of hampering free intercourse, and that in this case an equilibrium between countries with a high and those with a low standard of living is quite possible. In the third place the limits should be taken into account that are put to the ability of any country to pay interest and redemption on war debts and reparation payments, a problem discussed in chapter V

and to which we shall revert again in chapter X. The principle for the regulation of trade relations which follows from the above considerations is that an *approach to free trade conditions* is preferable.

If this procedure is followed, the perspectives for the future can even be called favourable. This is, if not proved, at any rate illustrated by the calculations of Colin Clark. This British statistician, basing himself on an extremely extensive material of figures and mainly justified methods of working, has estimated the extent of international trade in 1960[1]. In short, his method comes down to this. Starting point are the evaluations of the size of the future population of the different geographical regions of the earth. Next it is assumed, on the ground of what was ascertained in the past, that the productivity of labour in all non-agrarian branches of industry will keep on developing at the same rate as before. For it has been proved that this rate was not even permanently interrupted by the First World War. The productivity of labour in agriculture, in terms of industrial products, is dependent on the density of occupation of the soil; the greater the agrarian population density, the smaller productivity will be. Moreover, it depends on the price of agricultural products, expressed in those of industrial products. Clark now assumes that the distribution of the population over agriculture and the other branches of industry is regulated by the relative height of the incomes which can be drawn from these branches; accordingly, of the productivity of labour. From this distribution, which is consequently dependent on the price mentioned, the supply of agricultural produce can be deduced, while from the height of incomes their spending and hence the demand follows. Together they determine the price

[1] Colin Clark, The Economics of 1960, London 1942.

and at the same time the quantity produced and consumed in each country. If the production in any country exceeds its consumption, the surplus will be exported in exchange for industrial and other products from countries which are short of agricultural products. On the basis of this analysis the writer comes to estimated figures[1] for the world's trade in agricultural produce of the year 1960, from which we quote the following table:

WORLD TRADE IN AGRICULTURAL PRODUCE, IN MILLIARDS OF $ WITH THE PURCHASING POWER OF 1925-1934

Countries of Export	Exports		Countries of Import	Imports	
	1935/38	1960		1935/38	1960
Africa	0,63	5.15	Russia	—0.01	4.34
Central and South America (without Argent. a. Urug.)	1.29	3.67	U.S.A.	0.94	3.61
			Japan	0.25	3.12
			Gr. Britain	1.95	2.29
Balkan countries	0.09	1.76	Germany	0.75	1.17
India	0.51	1.38	Poland	0.01	0.74
Argent. and Urug.	0.62	0.72	China	—0.17	0.56
Western Asia	0.80	0.90	Netherlands	0.04	0.07
S. E. Asia		0.51	France	0.57	0.00
Java		0.33			
Other Ind. islands		0.83			
Total, incl. all others	4.90	16.10	Total, incl. all others	4.80	16.50

It will be seen that apart from of a strong expansion there are considerable changes in international trade between 1935/38 and 1960, if the tendencies assumed

[1] The figures are net for the group of agricultural products as a whole, i.e. the sum of surpluses of imports and exports of the separate products.

continue. They are chiefly the result of the expansion of industry in Japan, China, Russia and the U.S.A. Thus the high import figures of these countries can be explained. It stands to reason that these figures should not be taken seriously in every detail; all sorts of unexpected disturbances may occur. The disturbance of the Second World War is not likely to have been correctly anticipated bij Clark, who concluded his computations in 1941. The figures show, however, — and that is their importance for the subject in hand — in what way an equilibrium is possible between countries with a high and those with a low standard of living, notwithstanding the increasing productivity of labour both in the rich and in the poor countries, and in spite of the greatly increasing production in Eastern countries. As a by-result it is also interesting, e.g. for the Netherlands, that the price level of agricultural products as compared with that of industrial products will rise considerably and in 1960 will lie about 85 % above the level of 1935/8. Such calculations show us, even if they should have to be revised materially, that a favourable development of international production and trade is possible, and they also and especially show us where, i.e. in which countries and in which branches of industry, the lights in the development are to be sought, which also exist by the side of the shade to which everyone is so susceptible, and even in a preponderating degree. Consequently, even if there is reason to fear that an economic life left entirely to its own devices will again lead to crises and depressions — and we share this view — from the computations of Clark it appears what is possible under a certain guidance and an adequate instruction of economic life, and at what moment and in what direction intervention will be necessary. For that will have to be the case as soon as it appears that

actual production and actual exports, without any apparent reason, fall behind what is possible.

We have already made it clear that as a starting-point for affecting international commercial intercourse the situation should be taken that would arise under a free-trade system; this should serve as a 'model'. This does not necessarily mean that individual merchants should indeed be left entirely free, even to follow practices which in the past have proved to be the drawbacks to absolute freedom; a certain measure of organization, on the contrary, to prevent abuses, double work in propaganda and acquisition and too great variability is desirable. Such organizations have already sprung up from free industrial life on the one hand and from the governments on the other, and one should be open, at any moment, for new constructive proposals in this direction. It is also a good thing if great upheavals in development — owing to heavy foreign competition, whether or not arising as a result of new technical processes — can be absorbed or prevented by international consultation. All this need not derogate from the principle that no systematic fencing off of certain countries or groups of countries with regard to other territories must be allowed. Tariffs, prohibitions and quota systems should gradually disappear.

It is especially the fear of competition by countries with a low standard of living that must be considered as unfounded, prompted as it is by group-interests or by the slump mentality already mentioned. Besides the facts of newly arising branches of industry in these countries, which are competing with ours, there are a number of compensating facts which should not be lost sight of. In the first place these countries form a field of investment for the

redundant formation of capital in more prosperous territories and are consequently at the same time customers of a number of industries of means of production in the more highly developed countries. The U.S.A., Great Britain and Germany as well as, for instance, Holland are regularly exporting considerable quantities of capital goods to the less developed areas and this is nothing but a natural division of labour. Countries with a low standard of living also contribute in another way to the prosperity of other countries, namely by supplying cheap products, by which the cost of living decreases. Consider, for example, the cheap Japanese toys, bicycles, lamps and so many more products, which made it possible for these goods to come within the reach of much larger groups of the population.

Competition should only be fought with economically correct means; not by stupid fencing off. In this connection the raising of one's own achievements should be mentioned in the first place: the improvement of quality and the reduction of cost by more efficient methods of production. All this takes place regularly, and generally at a rate that has proved to be sufficient for a great number of years. In the Netherlands, for example, the productivity of labour in industry increased each year by 3 %, in the period covering the years 1929-1938. There have been countries, such as for instance Great Britain after 1921, that have not been able to keep up with this pace. This was justly considered as a point to criticize British industry, which was described as conservative and sleepy in many respects. Since then many new ways have been found also there — more intensive research-work in science and organization especially — to join in the race again with success.

A second means is a correct economic policy. In this connection its special task is to localize the occurrence of

temporary unemployment. If by the loss of foreign outlets unemployment is caused — say in the cotton industry — it will spread but for measures of economic policy and first affect engineering industry, which receives fewer orders from the cotton industry. In consequence of this depression in engineering, also other branches will now be affected, unless the government succeeds in compensating the slump in the engineering industry by giving additional orders. In this way the depression in the cotton industry can be localized, until new possibilities of production arise in that branch of industry itself or elsewhere by the normal increase of productivity.

A third way becomes necessary, if the collapse should be persistent and the increase of productivity insufficient to open up new export possibilities. Then the consequence of the apparently decreased achievement of the country should be accepted either by reducing the general wage level or the rate of exchange, in order to raise in this way the competitive power of the country again and enable the labourers that have been rendered idle to find employment again. About the degree in which this latter means can work, something at any rate is known from the experiences gained with devaluation after 1930. For five countries on an average it could be ascertained that a 10 % reduction of the rate of exchange resulted in a 7½ % increase of employment[1]. For Holland this would mean an increase of employment for about 100,000 men.

From several quarters it has been asserted — and this conception seems to have found many adherents in England, too — that the payment of high amounts for interest and redemption of war loans will make it necessary for the

[1] Cf. De les van dertig jaar, ch. 11.

countries concerned to curtail foreign trade, especially imports. Also this conception, however, is only to be understood from a slump mentality. We have seen that in a free-trade world the productive forces of every country are applied most efficiently; consequently the national product will be as large as possible; hence it is easier to effect a payment of interest and redemption from it than from the smaller production which is the result of protection in whatever form. We emphasize again that this only holds good when full employment of the productive capacity is guaranteed. In Great Britain it is intended to use every endeavour for this purpose. Then, however, protection is indeed unnecessary and can only be advocated by him who, consciously or unconsciously, takes a state of depression for granted. We may also argue in this way: by restricting imports, part of the internal purchasing power is prevented from applying to foreign countries. Then it is sure to appear in the home market. It there is full employment, this means that exports are reduced to the same extent as imports are reduced. Consequently nothing has been gained to obtain foreign exchange. Of course it cannot be denied that there is a certain limit to the paying-capacity of a country, if it is desired to effect these payments in money and that this capacity can be increased by supplies in kind. But this does not prove the necessity to curtail imports: supplies in kind signify by no means a form of protection of any country. In the light of these considerations it is not quite clear at present what people in Great Britain think they will attain by a regulation of imports, when at the same time they will try to realize full employment; an unconscious fear that it may not be possible to maintain this full employment presumably plays a part here. For the sake of international cooperation it is to be

hoped that, under certain conditions, they will be ready to reconsider this standpoint.

When in the above we have advocated an approach to free-trade conditions, this does not mean to say that we are pleading for a sudden abolition of all trade barriers. Sudden and extensive changes in the economic order usually bring about incalculable and in many respects harmful reactions. So the transition be gradual. For the rest, international trade is sure to be limited in many respects during the first few years after the war, which ties it will only gradually be possible to loosen. So there will be a natural breathing-space, in which trade and industry can prepare for the necessary adaptations, if the intentions for later are clearly formulated already. This adaptation can be facilitated by studying cost levels in various countries for a number of branches. Without further studies it will not be easy to foresee in which branches of industry changes will take place. Opposite the high wages in the U.S.A., which are the principal cause of the protective rates there, is the very high productivity of labour. It is sufficiently known that, in spite of these high wages, the U.S.A. can compete very well in the domain of the engineering industry and associated branches. In what other domains it will be impossible for her to compete is less easy to see and will have to appear from the studies mentioned. For the future export possibilities of other countries this point is of the greatest importance.

If it is possible, therefore, already to prepare one thing and another in the period of transition, the actual reduction of hindrances could moreover be spread over a period of say five to ten years.

Chapter IX

INTERNATIONAL MOVEMENTS OF CAPITAL

After dealing with the international intercourse of products in the preceding chapter, we shall now consider the intercourse of production factors. In chapter VII we already pointed out, however, that during the first few years after the peace treaty there can be little question of a movement from one country to another — in a direction that is justified from the social point of view — of the factors nature and labour, or in more ordinary terms, of territory and population. For this a sounder mental and political unity of the world is essential. Therefore, only the supply of capital by one country to another can be considered. It is on this that we will dwell in some more detail in this chapter; at the same time we shall then deal with the settlement of war-debts and reparation payments.

As pointed out in chapter III, the export of capital is a means to attain a certain measure of levelling in the prosperity of the various nations. A transfer of capital from say the U.S.A. to China means that the former country allows the capital quota in her production to rise a little less strongly than otherwise would have been the case, whereas the latter country attains an acceleration of the development of her capital quota. As a raising of the capital quota, as pointed out in chapter I, raises the productivity of labour, productivity in the U.S.A. will by this transfer develop a little more slowly than otherwise would have been the case and in China a little more rapidly. By a sufficient transfer of capital, therefore, a drawing together of the productivity

and hence also of the prosperity of these countries might be attained. I regard this diminution of the differences in prosperity as an important economic contribution towards the ultimate consolidation of the world's social system. At present, quite different problems prevail, it is true: the creation of a sufficiently strong governing centre and of guarantees for peace, also the finding, if possible, of a basis for cooperation between the Russian and the Western world are the principal of them. But they are not economic problems. It should be expected, however, that the large differences in standard of living between the Western world and the Far East will sooner or later lead to new tensions, for whose prevention every effort ought to be made. And in this connection a correct economic policy can have a great influence.

It will not be a simple matter to diminish the great differences in prosperity between East and West. It has been advocated simply to dictate to industrialists in the East to pay higher wages; hence a levelling 'by decree'. As to the incomes of farmers similar measures have been suggested. However, they will have a very limited effect only. For the root of all the trouble is that the production of these countries, per head of the population, is so small. If it should be dictated that higher wages were to be paid, the best employers would probably be able to bear this, not, however, the many working on the borderline of remunerativeness. These would be compelled to dismiss their workers, which would cause great unemployment and disorganize economic life.

It is theoretically imaginable that the prosperous countries should present a considerable and yearly flow of goods to the poorer ones: an international social policy analogous to the internal social policy in Western countries,

to be based on the consideration that the standard of living of the Eastern races is inhumanly low and that this is partly due to the fact that the Western countries are the big owners, especially of capital goods. For such a policy, however, the world is certainly not yet ripe; apart from the question whether this may be undesirable in other respects. It would be a more realistic policy to increase production in the Eastern countries themselves; then these races would, in a certain sense, help themselves, which is always a sounder basis for improvement.

In what ways is an increase of production attainable? There are three possibilities deserving our main attention:

a. raising the technical capacities of the population;

b. improvement of production-methods without raising the capital-quota: i.e. by a more rational arrangement of production, in the widest sense of the term;

c. increasing the capitals participating in production.

All three of these possibilities are already being applied in the countries meant; there is improvement in education, in technical instruction. The views on rationalisation, born in Western countries, are also penetrating there; and there is in those countries a formation of capital — though small — owing to which, also in their own strength, a heightening of productivity is reached. This process, however, could be considerably furthered in some countries, particularly in China and India, by international cooperation. In a country like China internal political order occupies a key-position: no economic prosperity is possible if it does not possess a minimum of stability, which, unfortunately, is frequently conspicuous by its absence. In the last decade, the war with Japan has, moreover, been a disintegrating factor of importance. Only when internal order has again been es-

tablished in China can it be hoped that the risks of capital investments have become so much smaller that their resumption may be anticipated. By international political cooperation the position of the Chinese government can be strengthened in the first place. Besides — and this is of great importance — the import of capital could be promoted by international economic cooperation; e.g. with the aid of a system of guarantees, to be given by the international authorities, to whose jurisdiction these matters belong. As such the newly created *Bank for Reconstruction and Development of the United and Associated Nations* is probably best suited, of which it may be hoped that it will become a powerful and well-managed institution. Through the possibility of such guarantees, which, of course, will not be granted to countries whose financial organization does not meet certain requirements, an educative instrument for this financial organization itself may be obtained at the same time.

In order to get some idea of the size of the capital movements that might be expected on the ground of what has been argued above, we ascertain in the first place what are the differences in rate of interest between the more and the less prosperous countries. In the following table some data have been collected:

Return of debenture bonds in %	1929	1932	1937
U.S.A. Treasury Bonds, currency > 12 years	3.60	3.68	2.68
Great Britain, Consols	4.60	3.76	3.31
China, Reorganization loan 1913	8.23	8.26	6.00
India, 3½ % government stock	5.27	4.75	3.82
Finland, state loans	7.7	8.4	4.7

It will be seen that the differences are considerable; they are attributable to at least two causes: to differences in

scarcity of capital and differences in risk premium. For a country like Finland it may be taken, certainly for 1937, that the last factor was absent; for India probably, too. For China both factors will have to be taken into account, for reasons explained above. The supposition that it must be possible by international cooperation to lower the rate of interest in China by 1/5 does not look fantastic in the light of the above figures. How much more capital would be demanded in consequence? Only the work of P. Douglas[1] gives information about the elasticity of the demand for capital; his results justify the assumption that this elasticity amounts to 4/3, i.e. that a reduction of the rate of interest by 20 % would lead to an increase of demand by about 27 %. Colin Clark[2] values the total capital invested in China at 35 milliard I.U.; the increase of demand by a 20% reduction of interest rates would then amount to 9 milliard I.U. For the sake of comparison we mention that, according to Clark's calculations, an annual import of capital might be reckoned with for the future of 3 to 4 milliard I.U. Hence it is evident that the extra capital import resulting from a reduction of risk-premiums is of an extent not to be despised. Should it be possible to push this levelling process still further — and in view of the above figure there is some ground for this — considerably higher figures might even be reckoned with.

Of course, these evaluations are highly speculative. They are based on very crude investigations and on tendencies which can only be ascertained in rough lines. We consider our evaluations just a sufficient motive for the necessity of a more thorough study of these problems. It

[1] P. H. Douglas, The Theory of Wages, New York 1934 and later work.

[2] C. Clark, p. 80.

may be observed that with regard to investment possibilities in the near East, including South-eastern Europe, similar conclusions are reached.

Particularly as to China the question is of importance which country will supply China with the necessary capital. Russia seems to lay some claim to the opening-up of China. In this connection we wish to point out that, according to Clark's computations at any rate, it is little probable that Russia will be able to raise the necessary capitals. It will almost entirely need for itself its capital formation covering the period 1945-1960 of about 175 milliard I.U., whereas the United States will be able to export about 60 milliard of their savings amounting to about 220 milliard I.U. It is logical, therefore — and in the interest of a levelling of prosperity — that the United States should have a large share in the development of China.

From the importance we attach to this supply of capital to the less prosperous countries it follows that we also consider the continuation of capital formation in the prosperous countries as necessary, or at any rate highly desirable. In the last few decades it has been argued that continuation and increase of this capital-formation is undesirable and superfluous. Those who have proclaimed these views mostly based themselves on a national standpoint; they did not consider the possibility of capital export or rejected it for one reason or another. Moreover, they started from the conception that a further increase of the capital quota in the internal production of the prosperous countries is either impossible or does not pay. The latter view need not be rejected. It is indeed imaginable that in the country that occupies a leading position in technical development, the new technical processes corresponding

with a further increase of capital structure are not yet known. It is likewise imaginable that a further rise of the capital quota is unremunerative. If there were no possibilities for capital export it would then be better, indeed, to form less capital and to use the released productive power for the production of articles of consumption. In other words, a larger share of the national income would have to be spent on articles of consumption and less would have to be saved. As soon, however, as there are also export possibilities, this is no longer the only solution. Then also less prosperous countries can in this way be aided in their development. And from the viewpoint of international stability the latter possibility is then preferable. It is also preferable because by it the total capital wealth of the world and hence the total possibilities of prosperity for the future are increased. Thus it means a certain sacrifice by the present generation in the more prosperous countries in behalf of the less thriving nations and in behalf of the future. So we have no objections to high savings in the wealthy countries, but on condition that they are not hoarded, as often happens in times of depression. For this means that part of the productive forces remain unemployed and that is on no account to be desired. Efforts should be made to avoid this by a good employment policy.

We find support for our views in the calculations of Colin Clark[1]. They show that for the continuation of the rise in labour productivity very considerable capitals will be required. These are estimated by him from the relation between the height of per capita production and the capital, per head, which he believes he can compute from his — very extensive — statistic material. If one takes these computations as a starting-point, the need of capital is even greater than the world savings that can be expected.

He computes these savings from the relation, as found in the past, between national income and savings. With an estimated total of savings between 1945 and 1960 of over 800 milliard dollars (having the buying power of 1925–1934), there would be a deficit of over 250 milliard. Should the disposition be continued to save less on a given income than before, his estimation of the savings would even be too high and the deficit in them still greater. Likewise this deficit would be greater than Clark computed it, if a correction is made in his estimate of capital requirements, for which there is certainly some ground in our opinion[1].

Even apart from the capitals which it will be possible to employ in the development of less prosperous territories, considerable capitals will be required immediately after the war for the reconstruction of the capital goods destroyed by the war. Besides this capital destruction the war has, for a number of countries, also led to very great national debts, which are partly of an international character. Among these international debts which, from the standpoint of a given country, can be added to the capital destruction in material goods, the lease-lend debts to the United States occupy a very important place. On June 30, 1944 America had, on the basis of the lease-lend act, granted advances to an amount of 28 milliard dollars, 9 milliard of which had gone to the United Kingdom in the form of goods, and besides that presumably over 1 milliard dollars in the form of services. On the other hand, there was reverse lend-lease aid by Great Britain of some 2 milliard dollars.

[1] It would lead us too far to enter here into greater detail. We have dealt with this problem in a discussion of Clark's book in the Revue de l'Institut International de statistique, 1945.

The United States themselves will be able to bear their capital losses caused by the war more easily than other countries, because these losses, as compared with their very great wealth, are smaller. Moreover, the safe geographical situation of this country has naturally prevented the destruction of capital by devastations. Only the diminution of stocks and the non-replacement of worn-out plant have to be recorded there as resulting from the war. Hence no country is in a better position to lend a helping hand to other states than exactly the U.S.A. Thanks to the fortunate circumstance of the safe geographical situation of their territory and of their great productive capacity it will be possible to reduce to smaller dimensions many of the disastrous consequences of the war. If the countries that have been particularly ravaged by the war should have to surmount in their own strength the results of these capital destructions, they would have to face almost insoluble difficulties. Their labour productivity has declined to such an extent that perhaps they would even be unable to produce a minimum standard of consumption goods; not to speak of a production, beyond that minimum, of the necessary capital goods for the reconstruction of their devastated plant and the replenishment of their exhausted stocks. They would consequently become 'depressed areas' in the world for a great number of years and exercise an adverse influence on the economic conditon of the world: for instance, they would be unable to resume their former imports to any appreciable degree. All this can be reduced to far less serious proportions, if the U.S.A. aid these countries — among which also Holland is to be reckoned — by supplying capital for their reconstruction. The old efficiency in production can then be restored rather rapidly and the taking up of these countries in a more

normal world economy is only a matter of a few years then. For a number of countries, however, this aid would result in new debts being added to those already existing, and the total amounts of interest and redemption which will then have to be raised by countries like the United Kingdom and numerous smaller ones, will be very considerable in proportion to the remaining items of the balance of payments. It is questionable whether such countries will be able to raise these sums without endangering the stability of their balances of payments and whether, in this connection, it would be in the interest of a stable and prosperous social system of the world to maintain them. If it is considered that the United Kingdom, instead of its foreign assets in 1938 of 3.6 milliard pounds sterling will have a debt after the war of at least an equally large amount, owing to which the item of interest and redemption will stand on the other side on the balance of payments — and will probably be higher — this is already a sufficient indication of the tremendous difficulties that are threatening. Therefore it would be an act of wise statesmanship if part of these debts were cancelled — a thing for which also in the U.S.A. voices have been raised already. Such cancelling is also in the interest of the United States itself, as otherwise it will compel the debtor countries to cut-throat competition in the export markets, of which it would thoroughly feel the reaction in its own exports. A cancellation may perhaps also be motivated in this way that, after all, the exposed situation of Great Britain, as well as the safe situation of the United States with regard to the foci of war, are accidental, viewed from the standpoint of world economy and world politics; they are no mistakes or merits of the countries concerned and therefore the debt-relation arising from them has no economic foundation.

As for the reparation payments to be made by Germany and her allies, similar, though not identical, considerations hold good. Also here it will be wise to be guided in the first place by the interests of a stable social world system with a prosperity as high as possible. Viewed in this way, the limits should be taken into account which, over a longer period, are put to the capacity of a country. If they are ignored, exhaustion will be the result, which will sooner or later revenge itself, also for countries which thought they could benefit by it. The actual limit put to capacity can be found by reducing the maximum production by what is needed (a) for a minimum subsistence of the population, and (b) for reconstruction purposes, as far as this is necessary to continue or resume production. In this connection it should be borne in mind that, if the standard of living of the population is put too low, this will automatically revenge itself in the level of production. Under high pressure it may be possible to dodge this law for some years, for a policy of longer duration it cannot be neglected.

We will illustrate our thesis with some figures. The value of Germany's production, measured by the national income, amounted to 82 milliard Reichsmarks in 1938. We may, for the average of the first five post-war years, reckon with a production of almost the same amount; then we shall probably be far too optimistic yet as to the speed with which productivity can recover. What, now, is the value of the minimum consumption of the German people that can be maintained for years at a stretch without undermining production? In order to estimate this amount, we consider that the Dutch people — which, by 1938, had about the same standard of living as the Germans — in 1943 already underwent a limitation of consumption, greater than could be maintained in the long run. This reduction

amounted to approximately 25% compared with the level of 1938. A reduction meant for a longer period, therefore, cannot exceed 20 %. As in 1938 about 3/4 of the national income was spent on articles of consumption, or 62 milliard Reichsmarks, a reduction of 20 % of that amount, or 12 milliard, will be possible. This amount would thus be released for reparations, except for the part necessary for the reconstruction of their own productive apparatus. For reparations could likewise be used the 20 milliard Reichsmarks, spent in 1938 on new investment and armament purposes. The devastations are now such that the reconstruction will take at least 20 to 25 milliard a year. Consequently 7 to 12 milliards remain for reparations, or say 10 milliards. We look upon this figure as a maximum, and expect that later calculations, which will only be possible when the actual situation is known, will yield a lower figure. This becomes all the more probable, if the disinvestments should still increase. Moreover, a figure is to be expected for the first two years that is far below the average of the first five years, and which might very well prove to be negative, which means that Germany would in reason be incapable of any achievement.

An amount, like the one calculated above, of 10 milliard Reichsmarks, could only be transferred by supplies in kind — or an arrangement equalling this; as we shall show in more detail (in chapter X), a transfer in money in the usual manner, leaving commercial intercourse unhampered, could only be effected for a small part. After the last war supplies in kind were not received with great enthusiasm by the receiving countries; the supplies of coal, for instance, were very soon felt as a competition for their own mines, and as a result they were crossed off the list after a few years' time. With a well-organized economic life this

competition need not be feared so much, but even then difficulties will remain if the supplies are too one-sided of composition. Only in case a great additional shortage has arisen of certain goods, which is sure not to be filled at short notice by home producers, will there be no objection to these supplies in kind. As is known, Russia claimed supplies in kind from Rumania in the form of work done by Rumanian labourers. It stands to reason that, in a country with great devastations, these can be usefully employed for a considerable time. Countries demanding reparation payments to high amounts should, however, be well aware of these difficulties and consider carefully whether they wish payment in kind. If not, they will have to be content, for the former reasons, with lower amounts than those mentioned above.

CHAPTER X

REGULATION OF FINANCIAL TRANSACTIONS

For a realization of the international economic aims discussed in chapter VI, not only the real economic relations between countries, but also the financial and monetary ones should be regulated. For from the latter may emanate, as was shown by the past, independent disturbing influences. It is particularly autonomous measures with regard to international payments, as taken by certain countries — and we are thinking of the devaluation of currencies as well as the putting up of all sorts of barriers by clearing, etc. — that have often caused great harm to other countries: this national, arbitrary procedure must be discontinued. As positive demands in this domain we can formulate: the greatest possible stability in the rates of exchange coupled with the greatest possible liberty in financial transactions.

The simplest theoretical solution would undoubtedly be the introduction of a *world currency*. By this is meant the introduction of one and the same currency for all countries, which consequently would be legal tender all over the world. All problems with regard to fluctuations in the rates of exchange would then become a thing of the past; it would not be necessary either to support weak currencies, and there would be no sense in a regulation of international payments by one country. In order to realize this ideal, however, the creation of this currency would have to be in one hand. In other words, only one central bank would be the real central bank of the world and the others only branch-establishments of it, or there would have to be such

intimate cooperation that the issue of money would be spread over a number of central banks. The cooperation would have to be very intimate, indeed! It would not be possible to tolerate that one country should, on its own authority, issue means of payment for too large an amount, owing to which the stability of the income and price relations would be threatened, also in other countries. Even too sharp discussions about the financial management might already lead to undesirable effects with regard to the confidence in the currency. If one thinks of the political relations of the moment — e.g. of Russia's desire so far to be economically closed — it will be clear that this world is not yet ripe for the introduction of a smoothly functioning world currency system.

Another possibility is a system of national currencies which are practically independent of each other, and consequently fluctuating with regard to each other. Apart from certain advantages concerning the possibility of adaptation to changed conditions, such a system shows many great drawbacks. The possibility of national arbitrariness is extremely great: the degree of confidence one could have in the fluctuating currencies of financially or morally weak countries would be rather small and the possibility of a disturbance of equilibrium would remain very great. In a way we have witnessed such a system after 1931, and, viewed internationally, it does not tempt to a repetition, except in case the economic policy of the great countries should remain far below the demands we formulated for it above. If in consequence of this every country itself must look after the best possible employment of its productive apparatus, fluctuating currencies may be unavoidable.

Viewed internationally, however, the preference should

be given to a system which on principle has the approximately fixed relation between the currency units in common with the gold standard, which can most easily be realized by coupling it with gold. For this purpose, as we shall further explain, also a measure of active cooperation is necessary, but this is within the limits of possibility and has, in fact, made good progress already. The coupling to gold need not have a quite unelastic character; it is imaginable — and has already become reality in the arrangements reached by the International Equalization Fund — that changes are allowed within certain limits when serious grounds can be produced. A country which loses part of its outlet through changes in international conditions and which, for social and other reasons, wishes to avoid a lowering of its wage and price level, can acquire new export possibilities by reducing its rate of exchange. Such a country should not be deprived of this possibility. It is desirable, however, that such adaptations cannot take place at any moment and to any extent, but are subject to certain limitations as regards time and extent. Thus it has also been arranged by the International Equalization Fund.

In this connection it is not necessary to think of the gold standard in one of its old forms only; at any rate, government bonds can also be accepted as cover by the side of gold, and for smaller countries also currency of the bigger ones, as for that matter was the case already in many countries. Naturally the advantage of the goldless standards is that then the improductive production of gold can be stopped.

The fundamental difference between the gold standard based on a pure gold cover, and a free standard for which — through poverty — only government securities are used as a basis, of which it is then said with some pathos that

it is a labour standard, is not so very great, as we observed already in chapter IV.

As we explained before, it is possible, however, to go much farther yet, and add to the means of cover other materials than gold; particularly a whole assortment of raw materials. It may be done in this way that 'parcels' of raw materials, of a fixed prescribed composition, are considered as equivalent to gold. Thus it might be attained that, within certain limits, the average level of the prices of raw materials would remain constant. For the stabilization of economic fluctuations this would mean a force to the good. The prices of the separate raw materials would not be bound by it; they could continue to indicate the relative scarcity position of those goods and by this continue to contribute to a sound automatic regulation of their production and consumption. Further it would not be necessary for all central banks to accept this cover — which is more difficult of administration — but only some of the greatest. Nor should it be thought that the raw materials would have to be present in kind in the banks: only the warehouse-warrants relative to certain stocks would have to be transferred to the bank.

In the case of one of the systems indicated above, which are more or less related to the gold standard, the rates of exchange would — but for some incidental changes — have to be stable. It is essential for this that the balances of payments are in equilibrium, both in the short and in the long run. This would be attainable by means of a complete regimentation of international payments, in the way that Germany knew before and many countries during the war. Owing to the many formalities connected with it and the consequent loss of time such an arrangement puts a heavy burden on the back of industrial life, which it will

be better to avoid. We would not advocate it as a normal condition; but the threat of it might have a great preventive effect. If speculative or other fitful capital movements should menace the stability of the rates of exchange, introduction of it might be necessary and also desirable. If, however, the remaining measures advocated here, are successful, the cause of such fitful capital movements will be considerably less than before and it may be hoped that it will be unnecessary drastically to restrict financial intercourse. These considerations do not hold good for a country like Russia, with a state monopoly for foreign trade; there payments are automatically subject to the supervision of state organs and the equilibrium in the balance of payments can easily be maintained.

For countries with a freer economic system a maintenance of the equilibrium for a short period is possible without special measures, if only they have sufficient reserves of gold or foreign currency at their disposal. In order to make this possible for all countries concerned, there should be a somewhat proportionate distribution among the various countries of the reserves available in the world, or it should be possible rapidly and simply to grant new credit to a country that is involved in difficulties. It is intended to meet these requirements by the establishment of the International Equalization Fund, owing to which also coordinated action is possible. It may be taken that no great difficulties will arise in this connection, as long as it is necessary to bridge over a temporary shortage of means of payment.

In order to prevent these shortages from becoming chronic, however, there should be an equilibrium between the items of the balance of payments in the stricter sense — consequently without the balancing items. As explained at

length in chapter V, it is by no means certain beforehand that, at a given position of prices, wages, production and rates of exchange, there will be such an equilibrium. It has been thought that the equilibrium can always be found by an efficient regulation of the rates of exchange, and for a number of cases this is even probable. In such cases it may be put thus that a certain currency is overvalued or undervalued with its existing parity and that by changing this parity the equilibrium can be restored. The normal case is that, when the payments annually due to foreign countries exceed the receipts from abroad, the currency concerned is overvalued and that devaluation can restore the equilibrium; exports — in their widest sense — will then rise more strongly than imports. However, we have also shown in chapter V that quite different situations may occur, when a reduction of the rate of exchange does not lead to a restoration of equilibrium, though it does lead, as it always will, to an increase of the volume of home production. Further investigations into the connection between the phenomena have shown us that, as far as the rate of exchange has any influence, it is in a way a secundary influence which it exercises. What is of primary importance — apart from exceptional cases — is that there should be monetary equilibrium within the country; in this sense that the incomes of the aggregate individuals and corporations are entirely spent on consumption goods, services and new investments, and that no hoarding or dishoarding occurs, with the latter of which creation of credit can be put on a par. All this to be conceived in this way that the dishoarding or creation of credit at any rate is not greater than what is necessary for a normal expansion over a longer period; in other words that no extreme inflationary policy is carried on, as was the case in Germany during

the years 1920–1923, and that no cyclic fluctuations occur in the hoarding and dishoarding. This latter demand, consequently, which applies to more normal conditions, comes down to a repetition of the demand for a correct trade cycle policy. This demand is, as we already pointed out, first and foremost a demand made upon the national economic conduct of the big powers. If this fulfils the conditions of a good trade cycle policy, an important factor to the good is already active for the small countries, too. In order further to assure also these countries of a stable economic position, it will moreover be necessary to make an end of autonomous changes in commercial policy (cf. chapter VIII).

Finally, a factor which does not belong to the normal economic picture, but one which will play a part of especial importance after the war, is that of the payment of interest and redemption of war debts and of reparation payments in money. When these payments — which we shall call 'unilateral payments', because their improductive character involves that there are no counter-items in the form of higher exports — exceed a certain level, monetary equilibrium likewise threatens to be disturbed and therewith the equilibrium in the balance of payments.

As in the relative literature, it is efficient here to distinguish between two difficulties that may occur. The first is the so-called transfer problem, the second might be called the difficulty of achievement.

The transfer problem consists in payments to foreign countries only being possible in foreign exchange, and — apart from the exhausting of stocks still present or the contracting of new credits abroad — this can only be obtained from a surplus of exports in the widest sense over imports. There are limits to this surplus especially for the

reason that there are limits to the value of exports. As we explained in chapter II, the value of exports cannot be increased at will or almost at will, as the classical theory would suggest; on the contrary, there are limits to the possibilities of increase. We get a clear idea of this when we start from the fact that a reduction of the price of export products by x % results in an increase of the quantity by $2x$ %[1] If we calculate for various price reductions what the total value of exports then becomes, we get the following table:

Price	Quantity	Value
100 %	100 %	100 %
90 %	120 %	108 %
80 %	140 %	112 %
75 %	150 %	112 ½%
70 %	160 %	112 %
60 %	180 %	108 %

All figures are expressed in % of the original values of the three quantities concerned. It is evident that there is a maximum value which is only 12½ % over the original value. If it should be assumed that the export quantity rises $3x$ as much in percentage as the price declines, the maximum appears to lie higher, but even then only 33 % over the original value. Statistical investigations having made it acceptable, as we saw, that the relation between the percentage of rise in quantity and the percentage of decline in price is under 3 rather than over, there are accordingly rather narrow limits to the increase of export value. Then it should be borne in mind that, when the quantity of exports is to rise considerably — in the above example by 50 % — imports will also have to

[1] The figure 2 then approximately represents the so-called substition elasticity of exports.

rise, owing to which the balance will become smaller than has been calculated. A closer investigation of possibilities shows that, consequently, the maximum of export balance depends both on the elasticity of exports and of imports as well as production, but that the above limits, as to relative size, give a correct picture of the situation. Regarding some more exact computations we refer to appendix I.

When by the side of these figures the amounts are placed which, at the present level of war debts, a country like Great Britain would have to pay, it becomes clear that much may depend on a correct regulation of these debts and their payment. The same thing holds good for the regulation of reparation payments, as far as they would have to be made in money.

The foreign assets of Great Britain had a nominal value of 3.6 milliard pounds sterling in 1938. In the beginning of 1944 1.75 milliard of it had been realized and had yielded only £ 1 milliard. The City estimated the value of the remainder at £ 0.5 or 0.6 milliard. On the other hand new debts had arisen to an amount of £ 3 milliard, besides the lend-lease debts of some £ 2 milliard; the total foreign liabilities would thus amount to £ 4 or 5 milliard. If for interest and redemption together 5 % is reckoned, a moderate percentage, this would mean a burden of 200 to 250 million pounds, against receipts of interest and dividends in 1937 of about £ 200 million! If it is considered that the value of imports and exports in 1937 was £ 953 million and £ 521 million respectively, it becomes obvious what difficulties a maintenance of these debts would entail.

Fortunately it is being realized already in expert and long-sighted circles in the United States that it is not in the interest of that country either to exact the full pound. For on the one hand it would endanger the monetary

stability of Great Britain — and with that of a large part of the world —; on the other hand it would compel the United Kingdom, its chief competitor in the world market, to launch such an export offensive that it would thoroughly feel the repercussion of that in its own export industries. When, moreover, one considers the origin of these debts, it is partly the exposed geographical situation of the United Kingdom against the safe situation of the United States; can these factors be looked upon as a serious foundation for financial relations in an efficient economic system? And how far, moreover, should the importance for America be taken into account of the political attitude of Great Britain at the end of 1940, then almost the only belligerent left on the Allied side?

If one views in the same way the transfer problem for possible reparation payments in money, to be made by Germany, it follows from the export figures for 1937 and 1938, which amounted to 5 to 6 milliard Reichsmarks, that such payments in money could not easily exceed an amount of 1 milliard Reichsmarks.

Such considerations hold good to a less degree if one manages to get round the transfer problem. This is possible by demanding payments in kind, as was done by Russia with regard to Rumania, which country, as has been pointed out, has to supply labour for the reconstruction of Russian territories[1]. It would also be possible by demanding supplies in the form of goods, to which this form might be given that the payments are at first made in money, but the stipulation is made that these amounts are to be spent in the paying country. The export surplus is then raised so much — if one likes: artificially — that the limits calculated

[1] This text was written already in 1944. The reparation claims on Germany have now also been given the form of payments in kind.

above no longer hold good. These only exist when the receiving countries are free where and how to spend the reparation payments. After the last war Germany made supplies in kind, e.g. coal; however, the receiving countries felt them as a competition for the national industry and after a short time they were crossed off the list. This feeling was based on an incorrect view, however; given a proper organization they could have benefited by these supplies without the chances of employment being injured by them. Generally it may be stated that, the better full employment is maintained by a correct economic policy, the better supplies in kind can be utilized.

In the case of supplies in kind, only the second difficulty mentioned before, the difficulty of achievement, makes itself felt in the paying country; this means, as we mentioned by the way in chapter IX, that there is a limit to the physical possibilities of supply. This limit is there where further supplies would lower the standard of living of the paying country so much that it would come below a human minimum. No doubt this minimum is a very vague idea, as the years behind us have shown clearly enough. By brutal force it is possible to press a population down to a standard of living which is considerably — perhaps even 50 % or more — below what was customary here before the war; a similar procedure, however, does not tally with our conceptions of humanity. A reduction by 30 % — corresponding with the level at which it is estimated that the Dutch population lived about the middle of 1944 —, already means an exhaustion at the expense of the future. Moreover, it should be borne in mind that also labour productivity is less at such a low standard of living, so that it is doubtful, even from the conqueror's standpoint, whether it is wise to go so far. Hence that in our compu-

tations of the preceding chapter, we believed we must reckon with a 20 % reduction of the living standard at most, from which we concluded — though with great uncertainty — that a capacity of much more than 10 milliard Reichsmarks cannot be reckoned with.

Separate measures against the 'vagabonding capital movements', which in the period of 1929-1939 caused so much trouble to the leaders of finance, are hardly possible, unless it should be considered advisable to proceed to a complete regimentation of international financial intercourse. As we observed before, we should prefer to see this used as a preventive threat only. This can be done all the better, if by a correct trade cycle policy in the principal countries, a curtailment of national autonomy in trade policy and in international financial policy, as well as a satisfactory settlement of international debts and reparation payments, many causes of instability and consequently of speculative capital transactions are removed.

It might be thought that a restoration of the gold standard or something akin to it signifies a return to 'laisser faire' and that by advocating this restoration the experiences of the period after 1919 should be ignored. This is not the case, however. If the conclusion is reached, as we did, that in spite of the existence of all sorts of possibilities for regulation in a certain domain, the condition of liberty should be approached as much as possible, because in that way the economic aims are served best, such a policy requires active supervision as to its observance. Formerly the governments did not know any better but freedom in financial intercourse was the only possibility. Now they have tasted of the honey of regulation and must

be kept away from it, which demands positive interference. This will accordingly be the task of the International Equalization Fund.

Important material decisions which the Fund will have to face are those regarding future parities. It would seem that, for the time being, the objective is to restore the parities of the West-European countries in the same relation to the dollar as existed before the war.[1] The measures for the French and Belgian francs and the Dutch guilder give ground for this supposition. It is possible that these parities are only meant for a certain time. Before stabilizing them, the governments should realize that the experiences gained after the last war with the restoration of pre-war parities, were far from favourable. We already pointed to the fact that the chronic depression in the United Kingdom after 1925, as well as the stagnation which production in Denmark and Norway showed about that time in comparison with Sweden and the world as a whole, is largely to be ascribed to the restoration of the old parities in those countries, after they had witnessed the development of a considerably lower rate of their currency during the first few years after the war.

If the rates of 1939 are to be restored without detriment to the volume of employment, certain requirements must have been fulfilled. A restoration of these rates would be justified in any case, if, first, 1939 had shown a well-balanced situation in this regard, and secondly, the changes in the conditions of competition had been equally great for all countries. There is room for doubt with regard to both these points. In 1939 there was in many countries a level of unemployment — though unequal — which

[1] Also this text was written in 1944. Since then parities have been fixed which are more in accordance with the views given here.

cannot be tolerated again in post-war years. And since 1939 conditions in the various countries have developed in a different way. It is true that the difference in the development of prices is not so very great, notwithstanding the fencing off of the occupied territories. The rise of prices in the Netherlands, for example, is not much greater than in Great Britain and the U.S.A. If the cost of living index numbers are put at 100 for 1938, the figures for the three countries are now 145, 140 and 130 respectively, and for wholesale prices approximately 160, 160 and 135 respectively. As part of the German economic area, and after it had once been adapted, the Netherlands showed a comparatively slow rise in prices — at any rate, as far as official prices are concerned —, but this was preceded by German quarters deliberately aiming at our insertion, which comes down to an increase of the former price-level by about 30 %. Originally the rise in prices was greater in the Anglo-saxon countries than in the German area, but since 1942 there has practically been stability.

Besides price movements there are other factors, however, which should exercise an influence on the choice of the future parity. For the United Kingdom, for instance, it should be taken into account that it is to expect a tremendous shift in its balance of payments against the pound sterling in consequence of the high war debts which it has had to incur. Unless a highly satisfactory settlement of these debts is reached, it will therefore need an increase of its exports, for which a lowering of the rate of the pound may be necessary. The Netherlands will presumably have to reckon with a serious decline in the purchasing power of its outlets, notably of Germany. On the other hand there is a possibility of more favourable export opportunities springing up for this country in the event of a freer com-

mercial intercourse. We do not intend to argue that from these few qualitative and incomplete observations it should follow already that a revision of parities is necessary, although a downward revision does seem justified. We only wish to point out that a more thorough investigation is highly desirable, in which the national interests of the countries concerned should be carefully weighed against the general, international interest. It is the task of the International Equalization Fund to make such an investigation, before they proceed to a more definite fixation of parities.

Chapter XI

THE NECESSITY OF AN INTERNATIONAL CENTRE

In the preceding chapters we have seen that in various respects a curtailment of national sovereignty is necessary with regard to economic policy, if a more stable and prosperous social system is to be realized in the world than we have witnessed since 1914. This curtailment of national autonomy is desirable in the field of commercial policy, in order to prevent the many arbitrary and unilateral limitations in international trade, which, notably since 1930, have caused so much harm. It is equally necessary in the domain of the technique of payments, in order to prevent arbitrary limitations in financial transactions as was done by the German regulations of foreign currency, or to prevent arbitrary changes in the rates of exchange of currencies of world-wide importance, such as the British pound or the American dollar.

We have also seen that international cooperation is desirable for a number of divergent purposes. Cooperation in the matter of a correct trade cycle policy is the first and most important point; cooperation in the management of an international currency reserve in order to reduce the risks of capital export and in an international control of cartels are some more forms, equally important. In the long run the countries will also have to come to the formation of a centre, from where the economic policy of the world is conceived and carried out, whatever the exact contents of this policy may be. It must be possible for the economic changes in world order which in earlier epochs could only

be attained by war, to be brought about in future by wise leadership and after public discussion, without war, if these changes are reasonable. Hitherto an organism was lacking for this purpose. The national centres of economic policy — the state departments of trade and industry of the separate countries — are naturally unsuited for this, because their task is the promotion of the national interests. The international centres which we have known so far were too much tied to definite, partial definitions of their tasks and, moreover, invested with very little power only. What is needed is an organism having the authority, on behalf of the international power centre, to take all the measures of economic policy which are necessary for the welfare of the world's social system, viewed broadly and for a long time, i.e. what Anglo-saxon writers have indicated as 'peaceful change'. Though the post-war atmosphere will probably not allow of this happening at once in that well-considered and undogmatic way which takes no notice of any group interests, it is to be hoped that it will be possible in the long run.

What I advocated above, even without these remoter objectives, comes down to proposing a certain regimentation of international economic life. I am now going to motivate this in some more detail. I am no advocate of a complete regulation of economic life in details and do not belong to the typical 'regulators'. Regulation within certain countries, apart even from what the war has brought, has possibly gone too far already. A substantial number of regulative measures has sprung up as a defensive weapon against the great depression of after 1929 and the hindrances to international trade resulting from it. If in future we may reckon with better regulated economic conditions in the world and with a curtailed sovereignty with regard to

commercial policy, a certain number of these measures can perhaps be done away with again. I am thinking of the regulation of agriculture in many countries, of the closing of certain branches of industry and of the restriction of production. I am therefore of opinion that some moderation in this respect may be welcome. However, if the regulation within the borders of the separate countries has perhaps gone too far, in the international field it is exactly the opposite. There is every reason to plead for more regulation there. This seeming inconsistency can be explained as follows.

In the first place there are forms of regulation which only have sense if they are international; think, for example, of the regulation of commodity markets, where competition has an international character. Nationally it is possible then to make shift by protecting the regulation with a tariff or quota-wall, but from an international point of view this solution is little satisfactory. In the past few decades this has been realized, too, and the most successful instances of market regulations — speaking purely technically, so apart from their purpose — were those where it had been possible to reach international agreement.

In the second place regulation in the international field is more urgent than within the borders of a country, because the existing situation in the international field generally shows more arbitrariness, in consequence of national sovereignty. In the preceding chapters, when discussing commercial and financial policy, we had again and again opportunities to remind the reader of this.

In the third place the lack of 'market knowledge' is much greater in international than in national markets. Compared with local and regional differences in circumstances, customs, etc. international differences are much greater, of course,

and thereby the chance of errors and wrong decisions. A notable instance is that of the capital market. It is far more difficult to judge of the remunerativeness of a new investment, of the measure of solvability, and of the dangers threatening it, in the international than in the national field; for this reason a system under which a guarantee is given by a mediatory authority is particularly desirable here.

In the fourth and last place it has appeared in our theoretical analysis, that exactly in the market which represents 'par excellence' the contact of every country with foreign countries, namely the exchange market, there is a special need of regulation, because here the price cannot under all circumstances perform its regulative function.

If, therefore, I am advocating a number of regulatory measures in the international field, the surprising feature in the results of our investigation has been that the concrete contents of these regulations have to be inspired by the 'liberal' theory to a larger extent than is sometimes thought. Particularly with regard to commercial policy and international capital movements it may be argued that the situation as represented by the theory of free exchange is, under certain conditions, the optimum situation, which is worth striving after. However, this conclusion stands or falls with the assumptions that it will be possible reasonably to approach a condition of full employment and that in the domain of politics international cooperation will be sufficiently close. Exactly because in the thirties these two assumptions had not been realized, it was logical that other solutions than those of the liberal theory were sought and found adherents in a fairly large circle. It is as logical, however, to revise one's opinion in the opposite sense

when the realization can be attained; on the condition of course, that full employment and international cooperation are also considered desirable in their effect. I think there is every reason for this. One need only read again the economic history of the Interbellum in order to realize what the alternative to international order means. It might be remarked that consequently I desire a return to the conditions existing before 1914 and that there was no conscious international regulation at the time; that, on the contrary, order existed and continued to exist 'of its own accord'. It may be replied that the resemblance of the aims formulated above with the conditions existing before 1914 is in various respects only superficial, but that, even if there is a resemblance in some points, it does not follow that also in the present world such a situation would arise again 'of its own accord'. As I already observed, there was a widely accepted notion in those days that the governments should refrain from any interference in the economic sphere; this is not so now; it has been found that it can also be done differently and the temptation to interfere is much greater for various groups of interests; at present a siruation as before 1914 can only be realized consciously, no longer unconciously, if I may use these words.

Therefore our considerations indeed prove the necessity of an international centre of economic policy. Considering the diversity of the subjects it will have to regulate, that centre can and must exist of different organs. It would have to be both an observation post and a centre of study, as well as — and this especially — an institution of guidance, supported by a proper power. This last point is all the more necessary as the interests of the individual states are looked after with so much more organization and purpose than, for instance, in 1919.

In discussions of experts or representatives of the United Nations a number of organs are already being prepared. We already spoke of the International Equalization Fund and the Bank for Reconstruction and Development; it is to be hoped that more such organs will be designed and that they may function well. Then we must also hope that the staff of the existing Secretariat of the League of Nations and the International Labour Office will be taken up. These bodies have given proof of being well-equipped for making investigations in the economic and social domains. Notably of late years they have published quite a series of important studies, which will be of great use for outlining future economic policy. These studies first of all refer to the trading policy as carried on by the principal countries in the period of 1919-1939, to the endeavours to get to a reduction of restrictions and the experiences gained from those endeavours about the technique of negotiations and the form of agreements. Other studies refer to the economic disturbances that arose after the last war and the conclusions to be drawn regarding an orderly transition of war production to peace production.

So far the organs have only been mentioned individually. It is obvious, however, that they ought not to act independently and therefore at a given moment perhaps in conflict with each other: their decisions must not be incompatible. Hence it is highly desirable that they should be vaulted over. Of this vaulting it may be hoped that it will develop into the seat of an all-sided international economic and financial policy, of which we spoke already by the way in this chapter: the centre that is to design the peaceful change of international society as far as economic matters are concerned, and that accordingly will learn to promote the general interest in contrast with

the interests of the separate countries and the interests of separate groups of producers and traders in international combination. It is beyond the scope of this book to enter into the question in what way it will have to be possible for the various national governments and groups of interests to exercise influence on the decisions taken by this centre. This question is part of the general problem of political cooperation in the international field, which we do not treat here. It must only be observed that expert knowledge for this work is essential and must not be subordinated to the representation of special interests. Both in the International Labour Office and in the Secretariat of the League of Nations experiences have been gained in this respect which do not call for repetition.

We conclude by expressing the hope that the work will not be done by halves, as in 1919. For once we may have an opportunity at present to achieve something. It is very doubtful whether history will grant us this opportunity again. It appears that the forces that can be unchained to destroy our civilization are so great that one gets the feeling: now or never!

Chapter XII

THE NETHERLANDS AND INTERNATIONAL ECONOMIC CO-OPERATION

The hope which always surged up again during the whole period of occupation and which, in spite of the arguments against it, became quite alive again during the liberation of Belgium, namely that Holland should get through the war without considerable devastations, has not been fulfilled. So we are now faced by the fact that, besides the exhaustion of our stocks and plant in the period of occupation, this country has been heavily damaged by the war. This naturally means that we have our work cut out as to relief and reconstruction work; may it be done with the necessary unity of spirit and also thereby quickly and efficiently. We shall not be able to do without international help. Thanks to the sacrifices of many, however, our prestige has certainly not suffered in the community of nations, and also on this ground we may assume that arrangements will be made. It is not the intention of this publication to enter into these arrangements of relief and reconstruction. Moreover, it would probably be too late already.

In this study we wish to speak of problems of longer duration, as, for that matter, has appeared from the preceding pages. For also these problems are already raising their heads: the work of reconstruction cannot be done quite independent of future possibilities. It is right, therefore, that the thoughts of many already go out to more remote periods: how about our possibilities of existence then? It stands to reason that for the Netherlands,

as a small country, this is a question with many international aspects; likewise that the questions of international economic co-operation are of great importance for our people.

Let us begin our discussions of these problems with the question, what position the Netherlands occupy in the community of nations. However much we have suffered from the war just now, it may be assumed that, thanks to our high degree of technical development, the quality of our soil and our trade relations, we shall, after a comparatively short time, be characterized again by what characterized us before, a fairly high standard of living — lying between that of most continental European countries and the Anglo-saxon world —, a less agrarian character than is usually thought — less than 20 % of our population works in agriculture —, and a national wealth invested for a relatively large part abroad and in Indonesia. Our imports form about 25 % of the value of the national product; they consist for a considerable part of the necessary raw materials for our industry, which is the principal source where our rapidly increasing population can find a livelihood. Our balance of payments was characterized by an import surplus, which was counterbalanced by receipts for shipping services, by interest and dividends. If a reasonable arrangement can be found for the foreign loans without which we shall not be able to do during the first few years after the war, there is every reason to believe that also these things will remain as they were, though the extent of our import surplus may have to become smaller. Hence comparatively large exports will be essential for the Netherlands.

In accordance with the economic structure of our country, free trade was always in its interest, also formerly;

likewise a well-functioning international financial system and good international cooperation. The Netherlands themselves practised free trade longer than any other country; it was not before 1933 that this country to some extent proceeded to quota-systems and to an increase of some duties. Then it defended the parity of the Dutch guilder with a grimness which was even detrimental to its own economic life; it was only in 1936 that it went off it, starting a depreciation which was the least of all countries.

Likewise there was always much interest, on the part of many kinds of experts, in international cooperation in other spheres than the economic. In contrast with this the interest in international politics, however, was smaller than might have been expected; in 1938 public life could to some extent be compared with a quiet island in an already boisterous ocean. Circumstances certainly have brought about a change in this respect, and it may be assumed that the Netherlands will draw the consequences in the matter of politics. It may especially be expected that it will be ready to put up with such restrictions of its national sovereignty as are desirable in the general interest. This has important parallels also in the economic sphere.

Compared with those of other countries, the prospects of Dutch exports are decidedly unfavourable for the near future, and doubtful for later. For the near future the destruction of our productive capacity makes itself felt as a factor on the side of supply. Our livestock is greatly reduced in number and underfed; we have hardly any pigs and poultry left. Our factory plant has partly been dismantled and taken away by the Germans, partly destroyed or insufficiently maintained and replaced. Rolling stock has been decimated; the railway bridges have been destroyed. Then there is the fear of increased competition

by the United Kingdom, which is in urgent need of enlarged exports in connection with its war debts, and by the neutrals, who are ready to start.

On the demand side the decrease in the demand for luxury articles will make itself felt, of which we produced a good many: bulbs, ornamental plants, grapes, chocolate articles. On the other hand it may be assumed that the demand for means of production (engines, harbour plant) and durable consumption goods (wireless sets) will grow. As to outlets, we shall have to reckon with a smaller demand from Germany, which was one of our principal customers (15 % of our exports in 1938), while also the situation in Indonesia will remain uncertain for some time to come.

For later years conditions may be viewed more favourably. Our productive capacity can be restored and the restrictions on the side of the supply will accordingly disappear for the greater part. As for agrarian exports, we may even hope for a favourable development. The computations of Colin Clark, quoted in chapter VIII, show that the demand for agricultural and dairy products, especially of high-grade types, is likely to develop favourably. This will become evident in the prices.

Clark calculates an increase of the imports of agricultural produce between 1935/8 and 1960 in:

Russia	of	4.3	milliard	I.U.
U.S.A.	,,	2.7	,,	,,
Japan	,,	2.9	,,	,,
Great Britain	,,	0.3	,,	,,
Germany	,,	0.4	,,	,,

From this it would follow — and it is not necessary to take the figures exactly in order to realize the probability of this trend — that it is advisable to develop our exports

to the first three countries mentioned. About the relation of prices (as compared with the average price level of industrial products) Clark states the following results: the prices of pork would rise by 70 %, of butter by over 30 %, of eggs by nearly 120 % and of cheese by 70 %. We repeat that these figures must not be viewed otherwise than as very rough estimates, dependent upon numerous factors the course of which is unknown. Thus it is possible that the mentality of industrial circles, particularly in the United States, will be in the way of a proper trade cycle policy and will reduce the possibilities for prosperity. But Clark's computations do take a number of the chief factors into account, the course of which *can* be foreseen with a certain degree of approximation. Up to now they are the best evaluations at our disposal. And they clearly counterbalance the too pessimistic expectations about the future of those who are overcome with the slump mentality.

Further it is evident that the Netherlands are greatly interested in a revival of international trade, and hence in a possible tendency to restore free trade. Should this be continued — and there are hopeful utterances from a number of prominent people in the U.S.A. which do not make it look quite illusory — it will also favourably affect the prospects for our trade. It would be an exaggeration to say that for our country free trade is a *conditio sine qua non.* If the trade cycle policy of the big countries should remain far below expectations, we should have to shift for ourselves and manage it, too. We have gained some experience in regard of quota-systems and currency manipulations, and could carry on a national economic policy. But the majority of the Dutch people would prefer to produce in a sphere of international free trade, and the country would certainly be better off. Various markets might then become

accessible again where we could compete in virtue of our achievements.

On the other hand, if we should live to see free trade more generally accepted again, the Netherlands should also cooperate loyally; it is our conviction that the country will do so. Not only with respect to the quotas within our European territory, but also to those in Indonesia. There is all the more reason to do this, because the exclusion of the cheap goods which in the Far East can be produced by our competitors, is against the interest of the Indonesian farmers, who with their small incomes cannot buy the comparatively expensive European goods. We must attempt to meet the competition of Japan, China and India by raising our own achievements, both in the foreign and in the home markets. As for the latter, there are still possibilities open. The educative work that has been done for some years past by a number of tradesmen's unions and by technical schools can be of great use in this respect.

If our own achievements should prove insufficient to face the competition of newly arising countries, a reduction of wages or of the rate of exchange would have to be resorted to. We already stated in chapter VIII that by a reduction of the rate of exchange an increase in employment, also for the immediate future, can at any rate be obtained, of sufficient volume to offset fairly heavy waves of competition. A reduction of wages can, especially in a slump period, unchain an unfavourable by-effect, which causes the results to be perceptible only at a later date. By coordinating such adaptations to altered relations of competition with a proper trade cycle policy, prolonged serious unemployment can be prevented and it can be seen to that Holland keeps the place in the commonwealth of producing nations to which she is entitled.

As far as the intercourse of capital is concerned, it may be taken that our country, after the work of reconstruction has been completed, will belong again to the countries exporting capital. The desiderata which we developed in chapter IX, if they are accepted as a line of action, then put on our country the obligation to contribute towards the evolution of the 'development areas' of the world. For the Netherlands matters are such that she can fulfil this obligation within the borders of her own empire. And this obligation appears under a particular aspect, now that the relation between the parts of the empire with regard to each other has again changed a little in consequence of political developments. Indonesia has made another stride towards the attainment of independency; it has somewhat less of the character of a colonial area again, somewhat more of that of a partner. The responsibility of the more prosperous part — the Netherlands — for the less prosperous part — Indonesia — will now be fellt all the stronger. Our task, to assure the population, especially of Java, of a life worth living, stands clearer than ever before us. Among other things, this will have to be attained by a further export of capital. The problem of industrialisation, as well as that of intensifying agriculture, should — now also as a problem of Dutch social policy — be studied more closely in this light, and the probable influence of a facilitation of capital-supply be ascertained. Then it should also be considered in how far the Dutch capital goods industry can be involved in the plans of development. If in this way the prosperity of the Indonesian population can be raised more rapidly, it is desirable to make also Dutch industry benefit by it.

Last of all, as regards international financial intercourse, there is not the slightest doubt that the Netherlands will be

ready to cooperate in any arrangement made for this purpose. It has even a distinct predilection for a solution which does not tie down financial intercourse too much. Our past has proved — we mentioned it already — that we were willing, even against our own direct interest, to play the game of the gold standard, when we stood almost alone.

We are certainly prepared to collaborate again on the basis of the new International Equalization Fund, particularly since the new parity of the guilder enables us to keep it stable. What we only hope for is that international cooperation will as soon as possible go into effect.

POST SCRIPT, AUTUMN 1945

The preceding chapters were written already in the autumn of 1944. The continued occupation as well as the paper and coal shortage in the Netherlands retarded publication. Many aspects of the problem of international cooperation have since got a more definite shape; many others are still as vague as they were before. A few remarks on the phase to which the long-term economic problems have come may be added.

In the monetary sphere things have become more definite by a choice of the parities for the French and the Belgian francs and the Dutch guilder. Fortunately these parities have not been chosen equal to their pre-war level: compared with the average sterling exchange rates in 1939 the French franc has been devaluated by 11 %, the Belgian franc by 26 % and the guilder by 21 %. As far as the guilder is concerned, it will certainly be possible to keep it on this level. Although there are, at the present time, some difficulties because of the decrease in labour productivity during the famine period, it will not be difficult to establish a new equilibrium between prices, costs and the present parity, as soon as regular imports of raw materials are resumed.

As to long-term credits some progress is also being made. Nevertheless, we must hope for a greatly accelerated development, if a really constructive international policy should be the aim of the United Nations. As with so many economic problems of the world, the key position is held by the United States. It is a supreme world interest that the immense productive machinery of that country can be kept running. For the near future there seems to

be some guarantee that production will go on. Many countries already gratefully absorb the flow of commodities emanating from it. In order, however, to have it continued, it seems that some fundamental changes in world financial structure are needed; and can we hope that public opinion in the United States will be ripe for them?

The problem to be faced before long — say one or two years — has been given this somewhat cynical formulation: how can the American government just present the other countries with annually say ten milliards of dollars' worth and yet make the American public believe they are doing good business?

This in fact is very nearly the real problem we are facing and the funny thing is that it actually is good business for the American people to do so. Throwing away ten milliards of dollars annually is presumably one of the few methods available for keeping the national income of the United States on a level, say, forty milliards higher than would otherwise be the case.

The International Bank for Reconstruction and Development seems to be the institute that is most appropriate for the performance of this task. What we must hope for fervently is an energetic guidance, by this Bank, of world development.

In the field of international trade a most important step has been the American decision to lower tariffs by 50 %. The need of an international centre capable to organise the spreading of this tendency is now being felt, however. Also here developments should be speeded up, if we are to use the chances offered. Quite the same is true for the supervision of international raw material markets. We cannot afford having a repetition of the events of 1919/1920

with their race for raw materials and the consequent boom in prices.

The most important spot of fatal uncertainty in world economics, however, is the German economic system. It seems that any elaborated and coherent plan as to Germany's reparation contributions, her volume of production and her standard of living is lacking. If so, we are evidently in urgent need of such a plan. If the Atlantic Charter is to be taken seriously and, consequently, European economic life to be brought on a humanly bearable level, a first necessity for the United Nations is to show what they are able to perform.

From these few remarks we may conclude, I think, that the urgent need for a powerful international centre is all the more clear. It is becoming clear too that if the United Nations should not succeed in establishing such a centre, it will be a vital necessity to the Western-European countries, Great Britain included, to collaborate on a more modest basis. These countries cannot, as the United States and Russia could perhaps, prosper by a system of autarky. In the absence of a world order they would have to try to come to a regional order at least. This collaboration would be purely defensive; and only a substitute for what they really want: an ordered world economy. We still hope, however, that this regional collaboration will not be necessary: that the new international organization will be vested with sufficient power and will attract sufficiently able men to start a new era. Seeing the task, the enormous possibilities and the urgent needs it would indeed be foolish not to take it up!

APPENDIX I

PROFESSOR GRAHAM'S CASE FOR PROTECTION

INTRODUCTORY

In the Quarterly Journal of Economics of 1923 Professor Graham[1] made an attempt to prove that, under certain conditions, international trade means a disadvantage to a country. His attempt concerns a country producing only two commodities, one under conditions of increasing, the other under conditions of decreasing marginal cost, of which the first is produced at a comparatively lower cost than abroad, the second at a comparatively higher cost. The statement was contested by Professor Knight[2] and there followed some further discussion[3], comment upon which was given by Haberler[4] and Viner[5] in their well-known books on the theory of international trade[6]. In the

[1] Frank D. Graham, "Some Aspects of Protection Further Considered", Qu. J. Ec. XXXVII (1922/3), p. 199.

[2] F. H. Knight, "Some Fallacies in the Interpretation of Social Cost", Qu. J. of Ec. XXXVIII (1923/4), p. 582.

[3] Frank D. Graham, "Some Fallacies in the Interpretation of Social Cost, A Reply", Qu. J. of Ec. XXXIX (1924/25), p. 324; Frank H. Knight, "On Decreasing Cost and Comparative Cost. A Rejoinder", Qu. J. of Ec. XXXIX (1924/5) p. 331.

[4] Gottfried Haberler, Der Internationale Handel, Berlin 1933, p. 149-156.

[5] Jacob Viner, Studies in the theory of International Trade, New-York—Londen 1937, p. 475-482.

[6] I have not found any comment on this discussion in: Bertil Ohlin, Interregional and International Trade, Cambridge, Mass. 1933 and R. F. Harrod, International Economics, London—Cambridge 1933.

discussion two points may be distinguished. First the question arises whether the case of decreasing marginal cost has much importance in practice. Most authors contesting Professor Graham's thesis hold that this is not so; the present author finds himself much in sympathy with this standpoint. Nevertheless the possibility of decreasing costs cannot quite be denied. The second point to be considered is, then, whether or not, and if so, under what further conditions, Professor Graham's statement is correct. In the present author's opinion, the main points in this question have, however, not or not very clearly, been met in the discussion and the comments. This appendix is an attempt to state the problems involved in a more exact way, with the help of analytical and graphical methods. After an exposition (§§ 1 – 8)[1] of the method and the author's own conclusions, a critical examination of the whole discussion is given (§ 9).

1. Measuring the 'advantage' to a country of international trade.

Strictly speaking it is not possible to tell whether or not a given country has an 'advantage' from the existence of international trade, since it is, on closer examination, not possible to give a precise meaning to the notion of 'advantage' to a country. It is possible to speak of an advantage to a single person; a given change in his situation brings him either to a higher or to a lower level of satisfaction (ophelimity). Since this satisfaction cannot be measured

[1] It may be observed that in the language of theoretical economics the case to be treated in these sections is that of isolated exchange between two individuals each producing two commodities. The individuals are, however, assumed to behave as in competitive markets.

and, a fortiori, a common measure for the satisfaction of the various subjects constituting a country does not exist, it is, however, impossible to add up the advantages or disadvantages for the single persons and hence also to give a precise meaning to the notion of advantage to a country. As, on the other hand, the discussion on the 'advantages of international trade' only has sense if some convention on this notion is accepted, we shall, in what follows, proceed as if a country as a whole also possesses a system of 'indifference curves', similar to those for a single person. We speak of 'curves' only and not of surfaces, etc., since we shall only discuss cases in which we have to do with two commodities 1 and 2, the consumed quantities of which, x_1' and x_2', determine the 'satisfaction' of the country $\Omega\ (x_1', x_2')$. Each indifference curve $\Omega\ (x_1', x_2') = C$ is constituted of (is the locus of) all commodity combinations x_1', x_2', that yield an equal satisfaction to a country. A combination x_1'', x_2'' yielding a higher satisfaction than a combination is situated on a 'higher indifference curve' etc. We make the usual assumption that these curves turn their convex side to the origin.

2. The possibility of decreasing and increasing marginal cost.

For simplicity's sake we assume that there is only one productive agent, which we call labour. The total quantity of labour a is given and is fully employed. The quantities used in the production of commodities 1 and 2 are denoted bij a_1 and a_2; hence

$$a_1 + a_2 = a \qquad (1)$$

The quantity a_1 depends on the quantity x_1 of commodity 1 it is desired to produce; likewise a_2 depends on x_2:

$$a_1 = \varphi_1(x_1) \qquad (2)$$

$$a_2 = \varphi_2(x_2) \qquad (3)$$

The functions φ_1 and φ_2 are called *cost functions*. Marginal cost in each case is $\varphi_1'(x_1)$ and $\varphi_2'(x_2)$, respectively; these expressions always have positive values. They may, however, be increasing or decreasing functions of x_1 and x_2. The case of *increasing marginal cost* is the normal case. *Decreasing marginal cost* for a whole branch of industry will hardly occur. Even if for a single enterprise the 'law of decreasing marginal cost' is assumed to prevail, it need not be valid for the industry as a whole. The law will, as a rule, only exist for certain intervals of the quantity produced in a single enterprise. It is a well-known fact that no situation of competitive equilibrium is possible within such an interval. If the branch is constituted of more than one enterprise, an extension of production will usually mean the necessity of using less productive units, i.e. increasing marginal cost. Only if the most economic size of the unit exceeds the size of the branch as a whole, will there be one enterprise; then, too, competitive equilibrium within the interval of decreasing marginal cost is not possible.

3. A GRAPHICAL REPRESENTATION OF THE EQUILIBRIUM OF PRODUCTION AND INTERNATIONAL TRADE.

In fig. 1 let x_1 and x_1' be measured along the positive part of the horizontal axis and x_2 and x_2' along the positive part of the vertical axis. The negative halves of these axes are used for plotting a_1 and a_2, respectively. In the fourth quadrant we draw the cost curve $a_1 = \varphi_1(x_1)$, assumed to be of the normal (convex) type. In the second quadrant the curve $a_2 = \varphi_2(x_2)$ is drawn in a similar way; to begin with,

it is also assumed to be convex. In the third quadrant the line $a_1 + a_2 = a$ is indicated, being the locus of all possible applications of productive resources. From these data the '*production curve*' may be deduced, indicating all combinations x_1, x_2 that the country is able to produce. This curve has the equation:

$$\varphi_1 (x_1) + \varphi_2 (x_2) = a \qquad (4)$$

Any point Q of this curve is obtained from the corresponding point Q' of the line (1) by the dotted lines in fig. 1. In the absence of international trade quantities produced x_1 and x_2 coincide with quantities consumed x_1' and x_2'. For its consumption the country therefore has to choose between the points on the production curve only. It will attain a maximum satisfaction if it chooses point A where the production curve is tangent to one of the ophelimity curves, plotted against the $x_1 - x_2$-axes: there is no point with a higher satisfaction to be found on the production curve. Under free competition this point will be attained automatically. The price relation between goods 1 and 2 will be indicated by the absolute value of the slope of the common tangent line to the two curves in P; i.e. that slope indicates the ratio between the quantity of x_2 exchanged for a unit of x_1; i.e. the price of x_1 in terms of x_2.

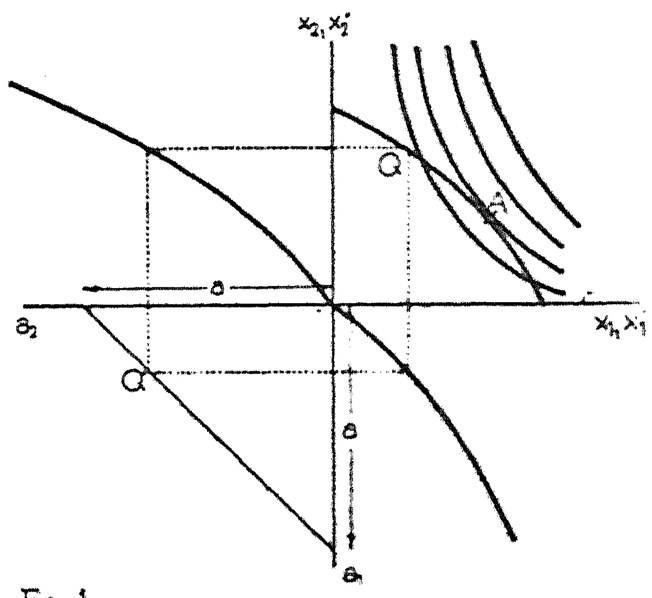

Fig 1

Now assume that an opportunity is opened to buy or sell in an international market at a given price p of x_1 in

terms of x_2, represented graphically by the slope of the line $R\,S$ in fig. 2, where the first quadrant of fig. 1 has been reproduced. This means, first, that no longer x_1 has to coincide with x_1' and x_2 with x_2'.

A 'consumption point' $x_1'\,x_2'$ may now be reached, different from the 'production point' $x_1\,x_2$ and connected with the latter by the equation

$$x_1' = x_1 + p\,(x_2 - x_2'),$$

indicating that the consumption of good 1 equals its production x_1, plus the quantity bought in the international market, at a price p, for a quantity $x_2 - x_2'$ of good 2; the consumption of 2 now being less than x_2. Of course also x_2' may be $> x_2$, but then x_1' will be $< x_1$.

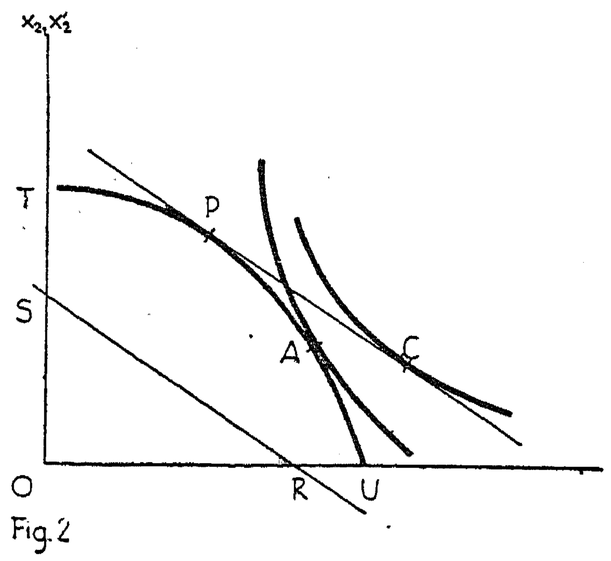

Fig. 2

Fig. 2 easily discloses what the new equilibrium situation will be. With the given price relation p producers will find it advantageous to use their productive resources in another way than before: in the case assumed in fig. 2, where p is lower than the price relation prevailing at point A, it will pay them to produce more of good 2 and less of good 1; equilibrium will be attained only if the marginal products obtained are of equal value. This means that they will proceed to point P, where the tangent line to the production curve is parallel to the given line $R\,S$. Having produced the quantities x_1, x_2, corresponding with P, the country is now free to exchange part of its production at the terms

expressed in equation (5), i.e., in graphical language, it is free to move along the 'price line' $P\,C$. This it will do until it has reached the point of maximum satisfaction, being point C, where $P\,C$ is tangent to an indifference curve. The new equilibrium is therefore represented by the two points P, C, the '*production*' and the '*consumption point*', respectively.

Under conditions later to be enumerated, *the satisfaction obtained in the new situation will always be greater than that obtained in the old one*. For, $P\,C$, as a tangent to a convex curve, will, for any value of x_1, show a higher value of x_2 than the corresponding point of the production curve[1]. Since the equilibrium point in the absence of international trade, A, is necessarily a point of the production curve, the satisfaction in C always exceeds that in A, except in the particular case where A and C coincide, i.e. where the price relation p in the world market equals the price relation existing without international trade. Hence, under the conditions to be discussed, *the introduction of international trade always means an advantage* to a country; with the exception of such 'boundary cases' where the advantage is zero.

4. Non-tangent price line.

This important conclusion was reached on a number of conditions, the influence of which we will investigate in the following sections. The conditions are:

[1] From P to the left, $\frac{dx_2}{dx_1}$ for the production curve is, in absolute measure, always smaller than $\left|\frac{dx_2}{dx_1}\right|$ for the price line; from P to the right $\left|\frac{dx_2}{dx_1}\right|$ for the production curve is always larger than $\left|\frac{dx_2}{dx_1}\right|$ for the price line.

(i) the production curve is convex;
(ii) prices are equal to marginal costs;
(iii) there exists a point P on the production curve for which the slope of the tangent equals the price relation p in the world market.

We shall first remove the last condition. It is conceivable, in fact, that the price prevailing in the world market is lower or higher than the absolute value of the slope of any tangent to the production curve; in the case of a convex curve this only means that it is lower than that slope for T or higher than that for U, the two terminal points of the production curve. In those cases the production point will coincide with T or U respectively; the conclusions drawn remain valid, however, as is easily read from the diagram.

5. Concave production curve.

Next we remove the first condition mentioned in section 4. This condition is closely connected with the nature of the cost curves assumed. If both cost curves are of the increasing marginal cost type, the production curve is convex. It may be convex too, however, if one of the cost curves is of another type. This depends on the degree in which the curve deviates from the normal type. We shall go into this question in section 6 below. Now we start from the other end and we assume that both cost curves are decreasing marginal cost curves. Graphically, this means that both these curves are themselves concave and it easily follows that also the production curve is concave (fig. 3). Now all points on the production curve, except the terminal points, are *unstable equilibria*. Extension of the production of one of the goods at the expense of the other always

means an increase in total value of production: the expanding industry gets more productive and the declining industry less productive than at the initial point.

If the opportunity of international trading is opened at a price ratio corresponding to the slope of a line $T\,V$, point T will be the more advantageous point and similar to what we discussed above (section 3) a consumption point C will be chosen. Generally point T will, in the presence of trading opportunities, be the production point if the price of 1 in terms of 2 is lower than the figure corresponding with the line $T\,U$, whereas U will be the production point if that price is higher than that figure. As an example of this latter situation, the price line $U\,C'$ is drawn, with a consumption point C'.

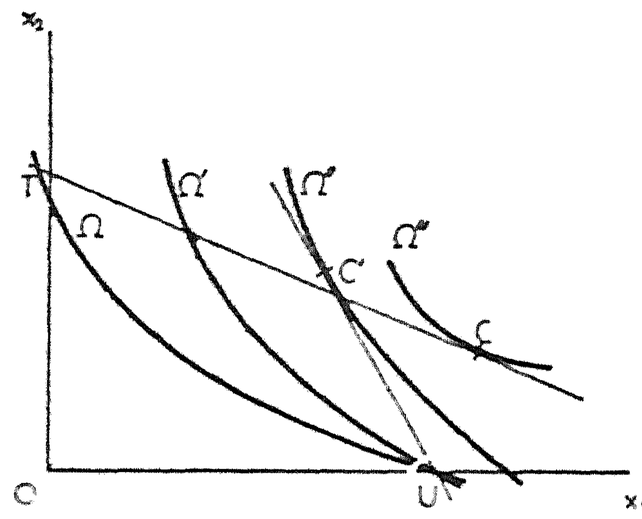

Fig 3

Again the conclusion can be drawn that the *introduction of international trade increases the satisfaction to be obtained for the country*, with the exception of possible (but not necessarily existing) boundary cases. One boundary case is the one where the price line through U coincides with the tangent to the ophelimity curve through that point.

6. A STRAIGHT LINE AS PRODUCTION CURVE; MIXED CASES.

As a special case, often made use of in simple expositions of the theory of international trade, we now consider the case where the cost curves are straight lines, the case of *constant*

marginal costs. The production curve is now a straight line too, of which each point is a point of indifferent equilibrium. Apart from this difference with the preceding case the same conclusions are valid. More complications arise if one of the industries operates under increasing and the other under decreasing marginal costs. It then depends on the exact form of the two cost curves, whether the production curve is convex, concave or of a more complicated type. If one cost curve is 'highly' convex and the other only 'slightly' concave, the production curve will be convex, etc. There may be intervals where convexity and others where concavity prevails[1].

In order to suggest that also in these cases of a 'mixed' production curve our statement about the advantage of international trade holds as a rule, we consider an arbitrary case of this class (cf. fig. 4).

For prices lower than the slope of $T\,U$ a stable production equilibrium will be found between U and S. The consumption point will be either at the exterior of the production curve or, in boundary cases, on that curve.

[1] A more exact study must be based on the analytical expression for these properties. An interval of a curve $y = f(x)$ is convex if $\frac{d^2y}{dx^2} < 0$ throughout that interval. In the notations used above we have:

$$\frac{d^2x_2}{dx_1^{\,2}} = \frac{\frac{d^2\varphi_2}{da_2^{\,2}} + \frac{d^2\varphi_1}{da_1^{\,2}} \cdot \frac{d\varphi_2}{da_2} \Big/ \frac{d\varphi_1}{da_1}}{\left(\frac{d\varphi_1}{da_1}\right)^2} = \frac{\varphi_2'' + \varphi_1'' \frac{\varphi_2'}{\varphi_1'}}{\varphi_1'^2} \qquad (6)$$

Since φ_2' and φ_1' are always positive, we see that $\frac{d^2x_2}{dx_1^{\,2}}$ is a weighted sum of φ_2'' and φ_1''; the weights varying along the curve. If φ_2'' and φ_1'' are of equal sign, $\frac{d^2x_2}{dx_1^{\,2}}$ has the same sign; if they are, however, of opposite sign, many possibilities exist.

Therefore, the satisfaction will be at least as great as before the existence of international trade.

For prices higher than corresponds to the slope of $T\,U$, point T will be one possible production point. The corresponding consumption point will lie on $T\,U$ and hence — apart from boundary cases — show a higher satisfaction level than in the absence of international trade.

This is not, however, the whole story. For some prices in this interval there are two equilibrium points. With a price only slightly higher than that corresponding with $T\,U$ there is a possible equilibrium point in the neighbourhood of U, since the production curve is convex also for some interval below U. The existence of two equilibrium points is nothing new: it was discussed in some detail by Koopmans[1]. It implies that, if by trial and error over small distances of the production curve, one of these equilibrium points is found and persists, the possibility exists that this point is not the absolute optimum but only a relative one. If we assume complete knowledge of all data with the economic subjects, they finally will choose the absolute optimum.

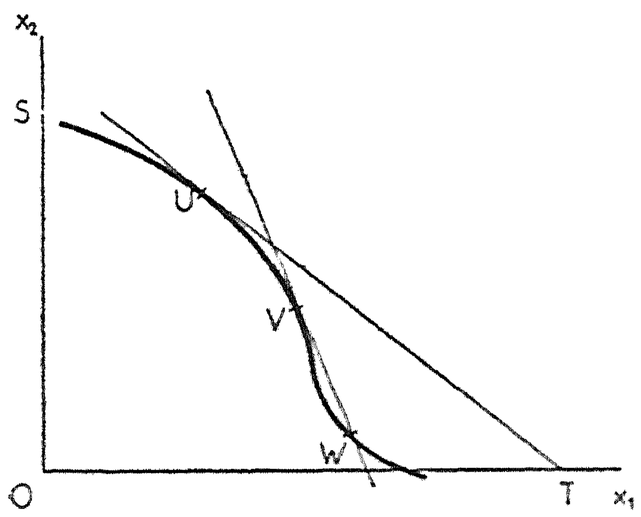

Fig 4

If that knowledge is not supposed to exist, they may stay at the lower, relative, maximum. In that latter case it may

[1] J. G. Koopmans, „De mogelijkheid van meervoudig economisch evenwicht", De Economist *81* (1932), p. 679, 766 and 841 and „Marginale kosten, marginale opbrengsten en optimale productie-omvang" in: Economische opstellen aangeboden aan Prof. Mr F. de Vries, Haarlem 1944, p. 149.

happen that the consumption point is one of lower satisfaction than the one prevailing before international trade was introduced. This case occurs if the course of the ophelimity curves happens to be such that the tangent point lies below W (cf. fig. 4). It then lies in the interior of the production curve.

Hence, *one condition has to be maintained in these mixed cases*: *the one of perfect market knowledge.*

7. Calculation of prices on the basis of average instead of marginal cost.

Finally we have to investigate the consequence of a removal of condition (ii) (section 4). This will appear to be a more serious threat to the validity of our statement. The necessity of assuming that prices are not equal to marginal costs of production only exists in the case of a decreasing marginal cost function. In industries where this law is valid, the equality of prices and marginal cost would entail a permanent loss to the producers. Hence it is probable that, in the long run, prices will be higher and in fact equal to average cost. In order to study the consequences of this hypothesis let us assume that industry 1 operates at decreasing marginal cost and that production is adjusted to its price in such a way as to make average cost equal to price. Since average costs are higher than marginal cost, this means that the

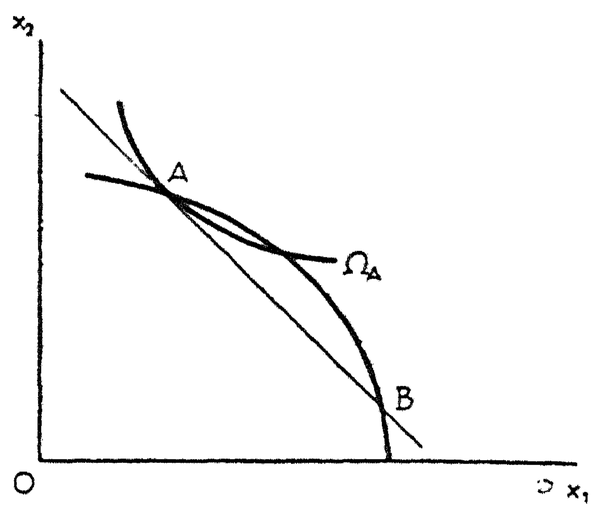

Fig 5

(absolute value of the) slope of the price line is now, in the equilibrium point, higher than the slope of the tangent.

Let us further assume that the production curve is still convex. In the equilibrium point without international trade a point A will now be chosen where there is no longer identity of tangents to the production curve and the ophelimity curve. The price line $A\,B$ now intersects the production curve, since its slope must be higher than that of the tangent. It is still a tangent to the ophelimity curve. This already means that the point of maximum satisfaction on the production line is not chosen: this way of calculating prices is disadvantageous to the country.

Now consider the case with international trade (fig. 6). Let $P\,Q$ be the price line and P the corresponding production point. There are two possibilities now, indicated in fig. 6 by the subscripts 1 and 2 and by full and dotted ophelimity curves respectively. In the first case, where the ophelimity curve through A, Ω_{A1}, does not intersect with $P\,Q$, the consumption point C_1 shows indeed a lower degree of satisfaction than A. Here *international trade is a disadvantage to the country*. In the second case, where the ophelimity curve through A, Ω_{A2}, does intersect with $P\,Q$, the satisfaction in C_2 is again higher than that in A and our former statement remains valid. Since both possibilities must be recognised, it follows that the removal of condition (ii) (section 4) is vital to our statement. Hence our general

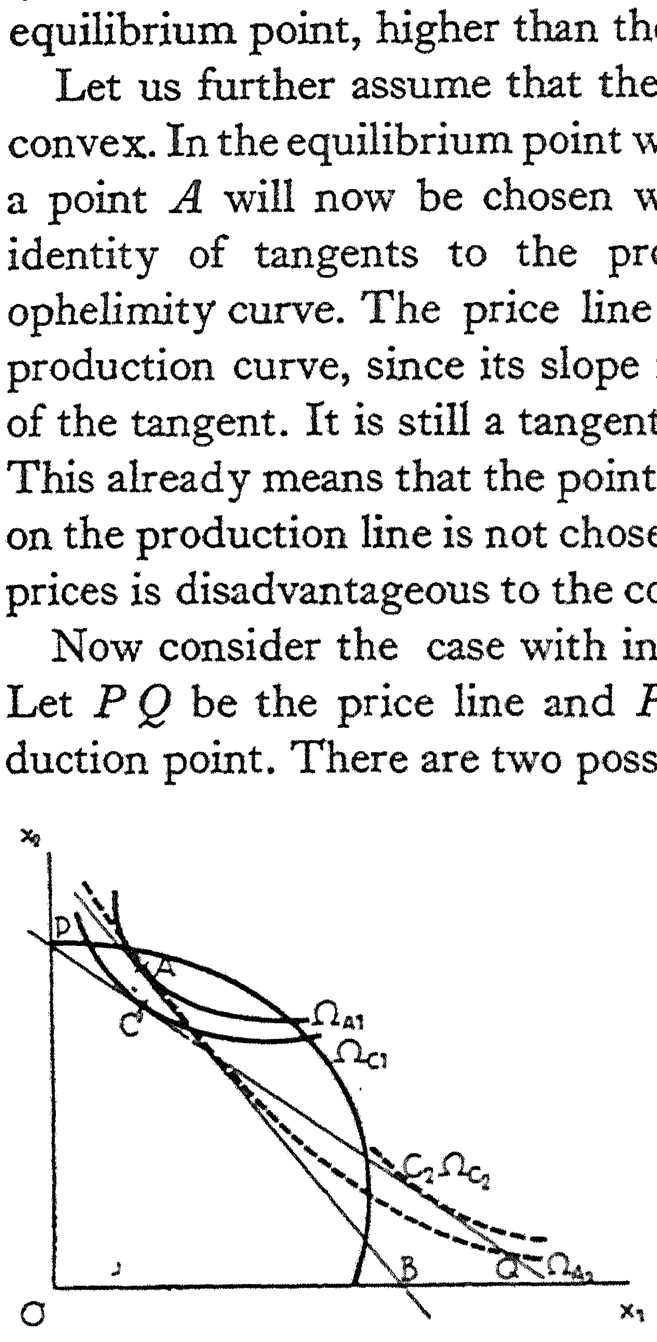

Fig 6

conclusions may be formulated: *in the simple case considered* (*two commodities and one agent of production*) *international trade is an advantage* (*or as a boundary case no disadvantage*) *to every country involved, provided that*:

1. *there is perfect knowledge of market data and*
2. *prices are calculated on the basis of marginal cost.*

8. A DIAGRAM FOR TWO COUNTRIES.

So far we only considered the position of one country finding itself vis-à-vis a world market with a *given price relation p* for good 1 in terms of good 2. We shall now try to answer the question *how that relation* itself is determined in the simplified case where there is only one other country in that 'world' market. It is by a simple extension of our graphical method that the answer may be given. In fig. 7, relating, as far as our first country, 'country A', is concerned, to the same situation as fig. 2, the co-ordinates x_1, x_2, x'_1 and x'_2 are, as before, plotted from the origin O, but in the opposite direction. The corresponding co-ordinates for country B, denoted by y_1, y_2, y'_1 and y'_2, are plotted from O'. The point O' is simply chosen in such a way that its co-ordinates with respect to O are x_1+y_1 and x_2+y_2, respectively, or, which is the same, $x'_1+y'_2$ and $x'_2+y'_2$. This implies that A's and B's production points coincide (point P) and their consumption points as well (C). A's ophelimity

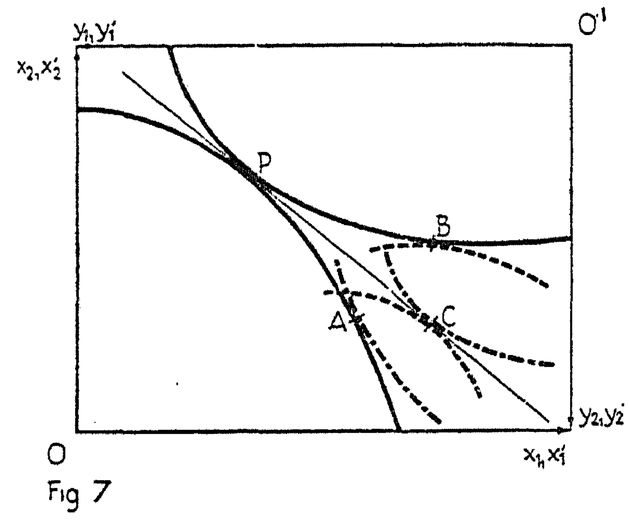

Fig 7

curves are indicated by —.—.—, whereas B's are indicated by — — — — curves. The points A and B are the production (and consumption) points of countries A and B respectively, in the absence of international trade. The essence of the graphical representation is that $P\,C$ is at the same time tangent to both production curves in P and to an ophelimity curve of each country in C. For the case represented, the one of convex production curves and point P for neither country in a 'boundary situation', the advantage of international trade to both countries is clear: the satisfaction to A is greater in C than in A and the satisfaction to B is greater in C than in B. The diagram cannot be constructed unless the position of C is given and this depends on the unknowns of the problem, viz. x_1. x_2, y_1 and y_2. Hence it might seem that the diagram is of no help in finding p. As a matter of fact, all these unknowns must be determined simultaneously; i.e. one must so long 'play round' with O' until a position is found where there exists — which is not generally the case — a common double tangent line to the system of ophelimity curves and the two production curves.

There are a great number of different cases as to the shape of the production curves and the situation of the production and consumption points; quite a number of boundary cases being among them. It may be left to the reader to go into these questions.

9. Conclusions.

We now propose, in the light of the foregoing analysis, to examine professor Graham's statement and the comments made upon it.

It seems that professor Graham gave his final standpoint

at the end of his second article. There it is assumed that in the world market (represented, in his example, by England) one unit of wheat is interchangeable for one watch. It is not stated how much wheat and how many watches are produced in the absence of international trade (our point *A*); so we may draw this point arbitrarily in fig. 8, relating to professor Graham's example[1]. The point reached after international trade has been introduced, our point *P*, corresponds to a production of 73,700 more units of wheat and 73,000 watches less than before. Professor Graham seems to assume further that the 73,700 units of wheat that are produced in excess of the original production are exchanged for an equal number of watches.

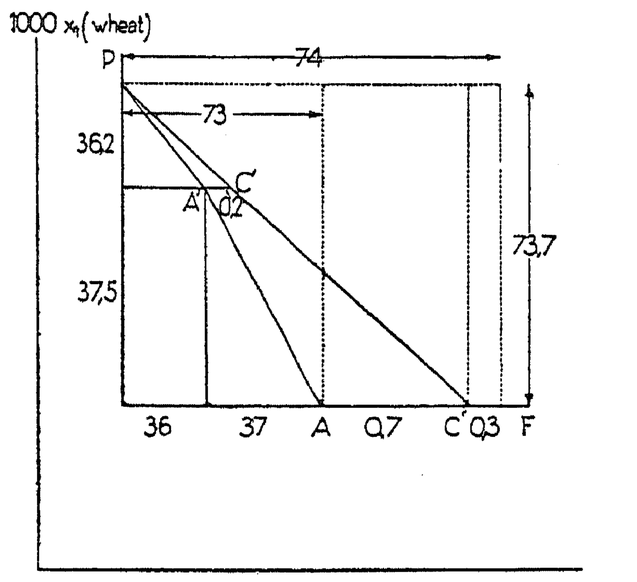

Fig. 8

Thus point *C* is reached (fig. 8). How now does he argue that the position in this point *C* is less advantageous to the country? 'The result of the whole trade — he says — is thus to secure 73,700 watches for the same effort as was originally producing 74,000 watches — a loss of 300 watches, to say nothing of the diminished returns to effort prevailing in the whole of the remaining American watch industry if that industry continues to struggle on'. This 'same effort'

[1] The true proportions of this diagram do not cover the figures; they have been chosen such as to show more clearly the convexity of the broken line PA'A and the relative position of the points A, C and F.

he is alluding to, relates to the productive agents producing the additional wheat; those agents were formerly engaged in watch making. The figure of 74,000 watches they were 'originally producing' is calculated on the basis of the *average* productivity of the watch industry then prevailing; not on the marginal productivity. In this way professor Graham introduces a fictitious point F to which he compares the point C reached after trade has been introduced; and then C appears to be less advantageous to the country than F. The real point of departure is, however, point A, and comparison should be made between A and C; it is at once clear that C is more advantageous to the country than A. The fictitious character of point F lies in the circumstance that the decrease in watches produced between F and P is calculated on the basis of the *average* productivity of watch making, whereas the increase in wheat production is computed on the basis of the *marginal* productivity of wheat growing.

This point seems to have been overlooked by Professor Knight as well as the other commentators. Knight does not go into the figures at all, although they were changed by Graham in order to meet his criticism. Haberler[1], after having literally cited Graham's conclusions, adds that one must concede that this deduction is right. Viner[2], when reproducing Graham's argument, changes the figures; apart from that change it is not clear whether the figures he assumes as the yield of one day's labour are meant as average or as marginal productivities. From the fact that he bases price ratios upon them, one would deduce that he means marginal productivities; from the fact however, that he calculates total productions by multiplying his 1 day

[1] Loc. cit. p. 150/151.
[2] Loc. cit. p. 476/477.

figures by the number of days worked, it would follow that he means average productivities. If the latter be accepted for a moment, his figures show an implicit contradiction, since he assumes that the total product of 399 days of wheat growing is less than the total product of 200 and 300 days. In other words, his example does not fulfil the condition that total costs of production cannot be a falling function of the quantity produced.

Of course, Viner himself is conscious of some of the ambiguities involved, but he fails to restate things in unambiguous figures. In another context, however, he rightly observes: 'Had Graham dealt with his problem in terms of marginal costs and marginal returns for both industries, he could not have obtained results unfavorable to free trade.' This indeed, as we have seen in the above analysis, is the crucial point, provided however, that, in 'mixed cases' (cf. section 6) perfect knowledge of market data is assumed for all subjects. It is to be doubted, however, whether the average reader of Knight's as well as Haberler's and Viner's exposition will retain this point as his chief impression; in particular that he will be aware of the fact that Graham may be right in the case of price calculation on the basis of average cost.

Appendix II

More exact valuation of the maximum amounts of unilateral payments that can be transferred

A first objection to the computation given in the text, as first made by Keynes in these discussions[1], is that the changes in imports have not been taken into account which occur in consequence of changes in price level, necessary to stimulate exportation. The simplest way to take these into account is by a mathematical-economic treatment. The following is an instance of this.

We indicate the volume of exports by u^e, the volume of imports by u^i and home production by u. The national price level be p, the foreign price level, measured in the currency of the country under consideration (whose rate of exchange is assumed as constant) p^w. We assume that the prices of exported articles are proportionate to the national price level, those of imported articles to the foreign price level. The value of exports U^e is then equal to $u^e p$, that of imports $U^i = u^i p^w$. We start from a situation in which there is equilibrium between import and export value, where consequently $U^e = U^i$. If a unilateral payment T ('tribute') is to be made now, U^e and U^i must change with amounts dU^e and dU^i, which are such that

$$dU^e = dU^i + T. \qquad (1)$$

Like Keynes, we assume that this change is obtained by a general price reduction of national products; the change in prices be dp; p^w will remain unchanged then.

[1] The German Transfer Problem, The Economic Journal, XXXIX (1929), p.1.

In consequence of this price reduction the volume of exports will increase; we put: $du^e = -\varepsilon^e u^e dp$, (2)
in which ε^e may then be called the elasticity of demand for exports.

Owing to the change in prices also the total production u will change; we put: $du = +\varepsilon u dp$, (3)
in which ε is the elasticity of supply of total production.

Imports will change likewise; they depend upon the price level at home (if this is low, imports are less remunerative than when it is high, taking it that all other determinants are the same) as well as upon the level of production. We put: $du^i = \pi du + \varepsilon^i u^i dp$, (4)
in which π is the import-quota of production and ε^i the elasticity of demand for imports.

Finally it follows from the definitions of U^i and U^e that:

$$dU^i = p^w du^i \quad (5)$$

$$dU^e = p du^e + u^e dp + du^e dp \quad (6)$$

We now consider dp as the unknown, the value of which is to be ascertained in dependency on the amount to be transferred T. The above equations enable us to do this. As we have the choice of the unit of quantity of goods still in our hands, we do it thus that the two price levels p and p^w are indicated in the original situation by the figure 1 (in other words: we express both price levels in index-numbers with the original situation as starting-point). Thus we get from (1), (5) and (6):

$$du^e + u^e dp + du^e dp = du^i + T \quad (7)$$

We now substitute (2), (3) and (4); we then get:

$$-\varepsilon^e u^e dp + u^e dp - \varepsilon^e u^e dp^2 = \pi\varepsilon u dp + \varepsilon^i u^i dp + T \quad (8)$$

As $\pi = \dfrac{u^i}{u}$ and $u^i = \dfrac{U^i}{p^w} = U^i = U^e = \dfrac{U^e}{p} = u^e$,

we can also write for (8):

$$dp(1 - \varepsilon^e - \varepsilon^i - \varepsilon) - \varepsilon^e dp^2 = \frac{T}{u^e} \qquad (9)$$

This is a quadratic equation for dp; for every value of T it yields two values for dp; but only in case T does not exceed a certain maximum T_M. This maximum can be found by putting the discriminant of the quadratic equation at nought; the result is:

$$T_M = \frac{u^e}{4\varepsilon^e}(1 - \varepsilon^e - \varepsilon^i - \varepsilon)^2 \qquad (10)$$

and herewith the maximum transferable amount has been found. This result passes over into Keynes' by putting

$$\varepsilon^i = \varepsilon = 0.$$

In order to be able to make a numerical calculation of $\frac{T_M}{u^e}$, i.e. the relation between the maximum amount and exports (for which we may take the value of exports, as $u^e = U^e$ in our units), we must know the three elasticities occurring in formula (10). As already stated in the text, we may put it that ε^e approximately $= 2$. Statistical determinations of ε^i have yielded lower values for this coefficient. We presume that values of $\frac{1}{2}$ and 1 are possible here. With regard to ε it should be observed that its value largely depends upon the degree of employment of the productive apparatus. If full employment is approached, then $\varepsilon = 0$, while with severe under-employment very high values may occur. From formula (10) it can be seen that, once $\varepsilon^e + \varepsilon^i + \varepsilon > 1$, each further rise of ε leads to a strong rise of T. In this is reflected the circumstance that in case of a strong reduction of prices, exports increase, it is true, but home production and imports decline. Owing to this also home consumption declines, and soon a point would be reached that, from

considerations of transfer, would allow of large payments, but would appear to be untenable from internal social considerations or even technically impossible. These are situations, where the transfer problem no longer forms the principal obstacle.

We believe we put our problem correctly if we attach the condition to it that there is a situation of full employment; then $\varepsilon = 0$. (A more complicated formulation in which attention is paid to wage changes as the primary factor and corresponding price changes, is to be preferred. It would lead us too far, however, to enter further into this question here).

In the following table the values for T and for dp have been brought together which correspond with $\varepsilon^i = \frac{1}{2}$ and 1, while we have taken $\varepsilon^e = 2$ and $\varepsilon = 0$.

ε^i	T_M	dp
$\frac{1}{2}$	$0.28\ U^e$	-0.38
1	$\frac{1}{2}\ U^e$	-0.50

From this it will be seen that already with $\varepsilon^i = \frac{1}{2}$ a very strong decline in prices would be necessary to attain the maximum calculated; from which it becomes probable that for technical reasons this maximum cannot be realized. The same thing holds good a fortiori in case it is taken that $\varepsilon^i = 1$ or $\varepsilon > 0$. Therefore our more exact calculations corroborate the argumentation given in the text.

Not much would change in these calculations, if, on account of a criticism made by Ohlin, another objection should be taken into account that may be raised against the calculations by Keynes. This objection is that Keynes

has overlooked the fact that the payment T leads to an increased income of foreign countries, resulting in an increased demand for export products from the paying country. Thereby exports already increase a little, even without a reduction in their price. Ohlin is even of opinion that consequently a reduction of prices is not at all necessary, and thinks that accordingly the transfer problem does not exist. This conclusion is wrong, in our view. The increase in the demand which arises in consequence of the increase of income T is only a small fraction of T, if there comes no change in the price relation between home and abroad. For a rise of income is spent first and foremost on home-made products and only for a small part on products of other countries, among which the paying country under consideration is only one. The fraction of T which is spent on products of the paying country will approximately equal the relation between its exports U^e and the total income of the foreign countries Y^w and this relation is a figure far below 1. Therefore our results will change only very little, if we do take Ohlin's criticism into account.

Appendix III

SOME NON-ECONOMIC CONSIDERATIONS WITH REGARD TO ANNEXATION BY THE NETHERLANDS OF GERMAN TERRITORY (CF. CHAPTER VII)

As was observed already in chapter VII, some proposals have been launched in the current year inside and outside our country concerning an enlargement of Dutch territory at the expense of Germany. In chapter VII we only discussed briefly some economic aspects of these changes of territory, faithful to the plan of this work. It is our opinion, however, that far wider than only economic considerations must turn the balance in judging these proposals; considerations which we can only describe as 'generally political': besides economic elements they contain elements regarding the technique of administration, military, social-pedagogic, historical and other elements, all of which are beyond the domain of the present writer. Hence the best solution can only be found by a cooperation of a large number of experts. The considerations to which we refer have, moreover, a far wider tendency than the argumentation on which the Dutch proposals mentioned above, are mostly based. The issue is not in the first place a question of reparations to the Netherlands for inflicted damage, but questions of the future stability of the whole of European life; perhaps even the saving of our civilization. A wrong solution of the problem how to deal with German territory and the German population conceals perils whose significance rises far above that of reparations; a correct solution can bring benefits which are of far greater importance.

The stability of European life and the survival of our civilization have been seriously threatened by the inhuman mentality of national-socialism, particularly towards the Jews, but also towards the opponents of their own race and in general with regard to the relation between man and the state, and between one state and the other. It is true that some of the national-socialistic notions are to be considered as a continuation of or a reaction to methods, applied and propagated by the Russian communists, but national-socialism is not exculpated by that: by these facts the responsibility of communism is charged as well.

The fundamental question to be considered after the war is: can the German nation as a whole be made responsible for the barbarities of national-socialism, or can only the bearers of that regime be considered responsible? No doubt the Germans are partly as much the victims of a series of coups d'état as we other nations of the continent of Europe. While they could still utter themselves freely, they were in a considerable majority against national-socialism. In order to ascertain the responsibilities, a thorough sociological investigation, under the guidance of first class experts, must be made, an investigation into the way in which the changes in Germany have been brought about, the importance for these of all kinds of institutions in that country and into the possibilities to prevent a similar procedure in future. In connection with this the essential question must be looked into, whether the German nation, under better leaders and with a better organization, is prepared and able to cooperate in a humanistic and stable Europe.

This problem cannot and must not be judged by politicians only. The development of sociology has got far enough to make us realize that only experts trained in these

matters can give well-founded advice. It is particularly in the United States, but also in Germany itself, that these experts are to be found. The investigation meant above should take place before a final peace-treaty is drawn up.

A priori widely different results of this investigation can be imagined. Both the view of old Clemenceau that the Germans are incorrigible and unable to live in a stable and humanistic Europe, and the opposite view that the majority of the Germans were themselves victims of their nazi regime, can be imagined as the result. The measures that will be needed are widely different in proportion as the one or the other result is obtained. If Germany should prove to be willing and able to cooperate, no unnecessarily harsh measures should be taken against a new Germany; then — after a period of transition, in which they can show their good intentions — it is even possible that a strong Germany is in the interest of Europe. Should it be unwilling or incapable of such cooperation, however, quite different measures may be necessary.

If cooperation is possible, a whole complex of measures is imaginable to make it stronger. This complex comprises economic as well as non-economic measures. It will, for instance, be useful to prevent wide-spread unemployment; sensible work will have to be found for ex-service men. Care will have to be taken that no new foci of infection spring up, such as certain unions of extremistic young men. On the other hand we should guard against awakening any kind of sickly nationalism. A division of German territory, however, might exactly further the growth of a nationalistic sentiment. If, therefore, the willingness in Germany to cooperate in a new Europe is strong enough, it is possible that such a division would exactly act in the wrong way.

But is may also be otherwise; if Clemenceau should be right after all, a division may have a beneficial effect.

What is essential, however, is that it is not the question whether the Netherlands require certain damages that is of paramount importance, but, as we said before, the much more important question how Europe is to be stabilized for the future. Also for Holland this latter question is of much greater importance. It is greatly to be hoped that those who, in this and other countries, will have to decide in these matters, will be well aware of this. We now need an internationally justified plan, well thought out in every respect, and no dilettantism prompted by temporary national interests.