

FORTHCOMING CONVERSATION WITH THE
UNITED STATES ON ECONOMIC QUESTIONS.

1. The primary purpose of the forthcoming conversations with the United States is to reach mutual understanding and discover a basis of common opinion. If we failed in this, if we parted company with feelings of suspicion, and without having made progress towards the definition of a joint policy, the disaster for us would be especially severe. Various alternatives are open to the Americans; but our plight will certainly be luckless and forlorn if we have to conduct our business after the war in the face of an un-cooperative and possibly even hostile America.

2. Alongside this primary purpose must be set what is no less important, the preservation and furtherance of our own vital interests. It would be altogether premature to assert that there need be any conflict between these two major purposes. On the other hand it is evident that the order and emphasis which we use in setting out matters touching our vital interests may greatly affect our success in dispelling suspicion and reaching mutual understanding. The whole scope of our agenda should be examined from this point of view and the order and emphasis prescribed in advance.

3. We have to recognize that there is some leeway to make up. Some suspicion already exists. Lord Halifax has frequently warned us; and we know it **independently**. The delay in signing the mutual Aid Agreement and the haggle over wheat have not helped. What is the nature of the suspicion? It is the fear that we may be too small-minded, narrowly self-interested and parochial in our outlook to be an easy partner in untried enterprises. Isolationist opinion is strong in America and there may well be a reaction to it when the war is over. Those of

them who want to adopt a more responsible and ambitious policy in World affairs must therefore be sure that they are on firm ground, that their would-be partner is truly like-minded, can appreciate their difficulties at home, and will not in some crucial issue stand on narrow ground and twist matters to her private advantage. Our American friends cannot run the risk of being branded and pilloried in their own country as having been "had for mugs".

4. All this makes for awkwardness. A great nation does not like to be put in the dock, to be tested and tried for its integrity, especially if that nation be one which has a certain tendency - such is our historic reputation - towards self-righteousness! That reputation may yet stand us in good stead. I do not believe that in order to meet American suspicion we have either to abate our demands arising from broad considerations of self-interest nor yet to make proposals, by way of gesture or token, in which we do not whole-heartedly believe. Rather it is a question of sorting out our own ideas, with a view to determining the proper order and emphasis. Progress has already been made; the important document entitled External Monetary and Economic Policy is a valuable contribution. But I think further progress is still possible.

5. One of our vital interests is the maintenance of our balance of trade after the war. This has bulked large in the discussions among ourselves. And rightly. We are entitled to consideration in this matter. It would be a poor return for our mighty effort in the common cause to be jostled out of our foreign markets and deprived of the means of paying for the imports which are so essential to us.

We are entitled to a margin over and above what is barely necessary. We cannot expect and should not desire an absolute guarantee of markets, for that would remove the spur to exertion and might usher us in to a phase of lethargy and decline. But we do need and must claim a reasonable opportunity.

6. But this, though essential, should not be the limit of our ambition. After all, before the war our trade was in balance; but we were by no means satisfied with our condition. Our export trade was subject to great fluctuation; we suffered from severe unemployment; successive setbacks in other countries made us altogether nervous about the future; the expansion of world trade which had proceeded for a century seemed to have encountered some new and obstinate forces of resistance. It should be part of our programme to overcome these forces and set the world economy on a better footing.

7. This world-wide economic disorder is a cause of concern to the Americans as well as to ourselves, while our balance of trade is a private problem. It is evident, therefore, that in conversations intended to elicit a common point of view we should begin with the subject that affects the vital interests of both countries and postpone the subject that is private to ourselves. Happily this order of procedure is already sanctioned by the Americans themselves; for in the wording of Article VII of the Mutual Aid Agreement, which can be taken as the basis of discussion, "action .. directed to the expansion .. of production, employment, and the exchange and consumption of goods" comes before the reference to the "elimination .. of discriminatory treatment in international commerce."

8. Furthermore until we have considered and agreed together about what action is required and what action is practicable to secure "expansion" and have made a rough sketch of how the world economy will appear when that action has been taken, it is impossible to form a judgement, that is worth anything, about how our balance of trade is likely to stand, or what special safeguards we may require in the long run. Therefore to raise this question at an early stage would not only show an unseemly egoism, thus confirming American suspicions, but would also lay us open to the charge of not taking the larger projects seriously at all. It would imply that we do not really believe that the larger projects will make any difference.

9. Again, when we do ultimately come round to our balance of trade, we may find it convenient, though this cannot yet be foreseen clearly, to raise it not as a private issue, but as part of the more general problem of what safeguards are needed for any country which has to import a large part of her necessaries of life. If it seems that liberty must be allowed for countries so placed to retain certain safeguards, the principle will apply to us automatically. That may prove a less invidious way of reaching the desired conclusion.

10. There are various methods of safeguarding the balance of trade position, e.g. by an agreed zoning of export markets, by an agreed specialization on certain types of commodity etc. One method which has received a good deal of attention in our preliminary discussions is what may most conveniently be valled the Schachtian system of trade control. (This name is less ambiguous than "bi-lateralism"). About this system opinion here is divided. It is now enjoying the vogue of a new-found weapon which we are using to good effect. But many think it must exhaust its usefulness after a short period

and would finally injure any country which employed it for long. Save under force or threat of force the customer countries would find means of escaping the helotage that it entails, and thus good export markets would be lost. We must not lightly repudiate the doctrine of multi-lateralism which is based on two and a half centuries of experience as well as common sense.

11. It is difficult to see how the Schachtian method could be an ingredient of an agreed international system; and it is probably for this reason mainly that the Americans very much dislike it. It rivets trade to politics and turns every new commercial development into an act of economic warfare.

12. Whether our balance of trade problem will require specific treatment cannot be known until we have more definite ideas about how the world economic problems can be handled. The Schachtian system is but one among various possible methods of specific treatment. Thus it is doubly far removed from those matters with which we should open the conversations. It is a special case of a special case. It is one among many remedies, dangerous in itself and of doubtful efficacy, for an illness for which we should now be hoping to find a preventative rather than a cure. It is a red rag to the Americans. It is widely condemned in this country. It would probably be obnoxious to our other allies and to the conquered peoples. We have provisionally foresworn it in the Mutual Aid Agreement. We should clearly not propose it for discussion save as a last desperate resource when all else had failed.

13. But the Americans may raise the subject at the outset. Knowing quite well how such it has been in our minds they may want a reassurance that we have genuinely repudiated it. Without this, they may feel that prolonged discussions would be a waste of time. There can surely be no doubt what our

answer should be. No final commitments are possible until the whole picture is filled in. They could not expect a one-sided commitment to be made in advance. But we should say that we earnestly desire to abandon the system as soon as possible and that it is for us a primary purpose of the conversations to find means of doing so with safety. To say less would be to commit a double howler. It would at once remove all sense that we are standing on common ground, for they will be unable to conceive - indeed who could conceive? - a pacific and fertilizing growth of interchange among a comity of nations, when one so important member contemplates the use of un-neighbourly and warlike tactics. And it would confirm their suspicion of us, since we should seem to be un-saying what we had so recently said in our signature of the Mutual Aid Agreement.

14. There remains the question of Imperial Preference. This has a double significance, as a symbol of Empire and as a method of economic adjustment. We may wish to retain it for its political symbolism and our right to do this should not be foresworn or even discussed in conversations on economic matters, provided that under this head we regard it merely as a token and not a major economic weapon, and agree to restrict it accordingly.

15. But we may also wish to retain it as a method of economic adjustment. Under this head it must clearly be subject to Anglo-American discussion. It may prove to be inconsistent with the plan for a general ordering of world affairs which emerges from our conversations. Or, it may happen that some kind of agreed zoning of markets is contemplated as desirable. In this case Imperial Preference may prove after all to fit naturally into the system. Or

again, some other method of zoning may seem better; in that case we should abandon Imperial Preference as a major economic weapon, not merely in deference to the Americans but because from our own point of view it would then be otiose. One point we must bear in mind. There is no doubt that the idea of a world New Deal appeals to the Dominions and that they will attach great importance to our achieving close collaboration with the Americans in bringing it about. They will have no sympathy with us if we fail to come to terms. Thus there is a real danger that by being too obdurate in defence of Imperial Preference we might lose an Empire.

16. So much by way of negation. But what should be the scope of our constructive proposals? What kind of action is required to secure an expansion of production and consumption? What is to be the nature of the World New Deal?

Certain proposals are embodied in "External Monetary and Economic Policy". Before I comment on them, I will consider the general background very briefly.

17. I have already referred to the malaise and doldrums which existed between the two wars. Each country, both on its own account and in concert with its neighbors, sought expedients for improving its internal trade and employment. But each country found itself impeded by shocks and disturbances outside. It seemed that purely national action was insufficient and that concerted action was required. But the political situation did not allow the execution or even the planning of concerted action. It is implied in the Atlantic Charter and the Mutual Aid Agreement that this country and the United States will take the lead in securing concerted action after the war.

18. To be more specific, the characteristic evils were disorders in the monetary system shown in great fluctuations of prices and exchanges and the uneven distribution of gold, lack of balance between the prices of primary and finished

products, an unprecedented fluctuation in the volume of world output and still more of trade, lack of investment opportunity, deficient adaptability of industry owing to immobility of labour, management etc., all this resulting in poverty in the midst of plenty and unemployment despite unsatisfied needs. I think these heads would appeal to the plain man, as well as to the expert, as covering most of the ground. A resolve by the two countries jointly to grapple with each of these world problems would implement the undertaking of the Mutual Aid Agreement to secure an expansion of production, employment, exchange and consumption.

19. Now it is the peculiarity of these kind of problems that the appropriate remedies, unlike piece-meal measures of reform, entail no substantial burden on the tax-payer. They are to a large degree costless or self-financing. What they do require is planning on a world scale, and sufficient world prestige on the part of those essaying to carry out the plan. The British Empire and the United States together have sufficient prestige, and the possibility of their working together thus presents a unique opportunity to scotch besetting evils and open a new chapter.

20. Some of these reforms could be executed by the unilateral action of the two great powers, all the co-operation that need be asked of other nations being to refrain from concerted sabotage. An example is an international bank, on the lines of Mr. Keynes' "Clearing Union", to deal with monetary disorders. Stabilisation in the prices of primary commodities could also probably be effected unilaterally. In the case of other problems willingness on the part of a number of countries to take concerted measures on advice or on the tender of a financial inducement must be presupposed.

21. I propose to imagine the establishment of an institution or group of institutions responsible for planning, advising and executing under each of the heads specified in paragraph 18 and to call it the Anglo-American Service. The nature of this service will be described more precisely below.

22. Some may hold that other countries should be brought into partnership in the Service and given a share of control, our other allies, for instance, or the allies and neutrals, or even all nations in the world. This is a political question which need not be discussed by the economic experts. It would be premature to discuss it now. Happily there is no need to await its settlement. The Anglo-American partnership should be strong enough to make a good beginning.

23. In the earlier period between the wars, before the international situation had so far deteriorated, great efforts were made under the auspices of the League of Nations, and otherwise, to improve economic relations. These were mainly directed to the removal or reduction of trade barriers. This is a consummation devoutly to be wished. At that time the efforts did not have much success; and there are objections to making such an approach the first instalment of a new order of co-operation. Countries are asked to take down the defences in which they have trusted, to remove protection, to undermine certain structures and throw certain workers out of employment. They are urged on by the philosophical and indeed **unimpeachable** argument that in the long run they will be re-couped and more than re-couped for their losses by the rising tide of world demand. The argument is correct, but uncomfortable and austere. It would make an unhappy inaugural address to the new comity of nations.

24. Furthermore it is widely and correctly held that the removal of barriers by itself is not enough. It needs to be supplemented by the constructive tasks of the Anglo-American Service. It would be wise therefore to make an announcement of the service the first instalment in the programme of reform.

25. If these views are correct, our proper course in the Conversations is clearly indicated. We should press hard for the Anglo-American Service; that is for a number of reforms which I have grouped together under this title. We could do so with dignity and, I hope, conviction. The fears and suspicions that our point of view is too self-centred would be dispelled. Indeed if we are forthcoming and even rather bold in our proposals we might make the Americans take the role of cautious critic. That would be of immense advantage to us; when two parties are seeking accord it is the critic who has the more uncomfortable and thereby weaker position; we should put ourselves right with the Dominions; and we should greatly strengthen our case in demanding special safeguards, if that proved necessary at a later stage.

26. Opinions no doubt differ in America, as elsewhere. The State Department may lay greater emphasis on free trade, representative New Dealers on more positive and constructive measures. We should of course be most "receptive" to proposals for freeing trade and will hear with interest what tariff concessions on the American side are thought feasible.

27. Anxiety has been expressed lest we proceed some way on the path of reciprocal concessions and then find our plans brought to nought by American unwillingness to implement them, owing, for instance, to a change of Administration there. By making the concessions mutually dependent, we should avoid all risks of suffering actual injury. But still, we do not wish to be left with all our plans in the air. The danger is greatest in the case of tariff concessions; and we should put a curb upon our hopes. The danger is less in the case of the Anglo-

American Service, and this is a further reason for pressing it strongly. It ought to be possible to arrange that the Service should impose no substantial burden on the American tax-payer, nor interfere with his liberties and privileges, nor raise party issues. It would be a very drastic measure for a new Administration to dissolve Anglo-American institutions already in being; and it should be possible to bring them into being within the certain life-time of the present Administration.

28. All these arguments in favour of the Service would have been valid and cogent had such an opportunity for Anglo-American leadership occurred before the war. Now a new gravity has been added to them. The word has gone out that "this must never happen again". That word must be fulfilled. The horrific possibilities of the most modern science should make our resolution as grim as death.

29. But how is the word to be fulfilled? Anglo-American accord must be maintained in the face of the tremendous tendency in human nature to fraternal bickering. Responsibilities and burdens must be undertaken by the two peoples. Will their legislatures be willing to go far enough? Policing must entail interference with national sovereignties. Will there be general consent to this? Shall we have the vital energy to make it permanently effective in the absence of consent?

30. This world responsibility has its economic side. Paradoxically, but happily, the task of economic surveillance **so far** from adding to our burdens should make the political tasks easier. The economic Service is twice blest; it should benefit the powers undertaking it as well as the other nations. If the same powers which take the lead in enforcing an unwelcome policing discipline are seen to be responsible for immediate and tangible economic benefits, the discipline may be

more readily accepted. Policing must involve some interference with sovereignty; the economic Service need not. And on our side if what the legislatures have to vote in setting up the Service involves no substantial burden on constituents and may be shown to be of great advantage, they should do so without demur. But having built one part of a fabric of Anglo-American condominium - and this economic part can be done during the war - they may the more easily be led along to endorsing joint enterprises that are not so painless. Again, the economic Service would provide practice and experience in co-operation. We already have co-operation in war; if to that is added the beginning of co-operation in the economic tasks of peace, the final step to joint peace-time policing should not be so difficult.

31. I must now return to the proposals of "External Monetary and Economic Policy". How far do these go in giving body to the idea of an Anglo-American Service and in covering the problems specified in paragraph 18 above? Do they deal with the whole agenda constituted by Article VII of the Mutual Aid Agreement?

32. The two principal proposals on our side are (i) the "Clearing Union" put forward by Mr. Keynes and (ii) the plan, referred to in paragraph 18 but not yet set out, for "steadying the prices of primary products and the holding of buffer stocks". There are references to expected American proposals. And there is a rudimentary sketch in Appendix III (me auctore, this description involves no breach of manners) of an Anglo-American investment board; it is not clear, however, if Ministers are asked to give this plan their blessing. Prominence is also given to the proposal that capital movements ought to be restricted; but this belongs to a different category (see Annex I to these notes).

33. The two major proposals are admirable in conception. Alone they are not sufficient to complete my idea of an Anglo-American Service. Nor do they cover the whole Agenda of Article VII. There is a tendency to wait and see what the Americans will put forward. This casts us for the role of critic which, in my judgment, is injudicious. Moreover the Americans may be hatching plans to which we are bound to object. We shall be in a very weak position if we have not an ample reserve of counter-proposals. It is too late now to work out anything fresh in detail; but I think that there is a way in which this difficulty may be overcome.

34. If the two major proposals were put forward in isolation, there is some danger that they might be misconstrued. The Americans know that we are worried about our balance of trade and that we are reluctant to pay what they regard as a proper price for wheat.

Might not the Americans think that we are still thinking more of our private and perhaps petty interests than of the world balance, that the Clearing Union is merely putting a grandiose international facade onto the request for a little credit and that the elaborate international commodity scheme is but a ruse for shuffling out of our wheat commitment and avoiding a fair deal on cotton? I think that both schemes are intrinsically just and necessary, and that the suspicion may be obviated if they are put forward in the right order and with the right emphasis.

35. One principal purpose of the Clearing Union is to regulate the relations between creditor and debtor countries. This badly needs doing. To make the Union an efficient instrument for this purpose the bracketted alternative under 85(4)c should be made binding and brought into full prominence; I have explained this in Annex II to these notes,¹ Essential though this regulation is, for world

¹ I understand that there is no objection in principle to my amendment.

order, yet it must be admitted that it bears intimately on our self-regarding anxieties and to that extent provides a bad introduction to the discussions.

36. But there is another aspect of the Clearing Union. It is a bank. As such it will have resources. As the world central bank it should have great resources. And thus it may give financial support, indeed may be regarded as the financial corner stone, for the congeries of functions which together make up the Anglo-American Service. This point is taken in paragraph 15 of the Memorandum. I should lay the greatest emphasis upon it. It justifies the attention which has been given to this particular scheme and the detail in which it has been worked out. After all we have not had much time to prepare for these conversations; we are pre-occupied with the war effort; we cannot be expected to come with cut and dried schemes covering a vast field. But because this particular scheme is the corner stone of the whole we have felt it necessary to lavish more thought upon it. And for the same reason we suggest that it be given priority in the discussion. From this point of view I could wish that it were called a Bank rather than a Currency Union or a Clearing Union; a Clearing Union suggests a mere channel; a Bank has the wherewithall to make advances.¹

¹. If the Clearing Union confines itself to Clearing, it would have its liabilities (credits) backed to the extent of 100% by assets of perfect liquidity; for it is only obliged to convert bancor into the currencies of other countries. But this backing is unnecessarily large. It should therefore be able to make advances on a considerable scale.

37. The Memorandum introduces its plan for commodity regulation (paragraph 18) by referring to the American Administration's pre-occupation with this subject. It is certainly wise to have counter proposals ready; and we may admit among ourselves that we fear further American price raising plans. But this should not be our main motive, esoteric or public. Whether we look at Article VII or paragraph 18 of these notes, it is evident that the Trade Cycle should be a dominant theme in our discussions; it affects all our plans. In my view reduction in the oscillation of farm prices and incomes would be the most effective single measure for mitigating this evil.

38. Conquest of the Trade Cycle is a well-worn subject on both sides of the Atlantic; many proposals should be forthcoming with regard to it. But in so far as they are connected with public works and public finance, specific remedies cannot be suggested without a prior study of the special conditions in each separate country, and they will depend on the collaboration of each country. But the regulation of primary commodity prices may be applied uniformly on a world scale by the unilateral action of the British Empire and United States. I suggest that the Trade Cycle should be given high priority in the order of discussion; and that great emphasis should be laid on the eligibility of the commodity scheme for early execution as part of the Service.

39. Thus there are good grounds for giving priority and emphasis to our two schemes, to the Clearing Union because it is the corner stone, and to commodity regulation because this is the biggest single remedy for the Trade Cycle that can be applied by unilateral action. But the case will only be convincing if we seem to mean

business in regard to the whole range of problems, and we certainly shall not seem to mean business if we treat these two schemes as a sufficient contribution to their solution.

40. But if we have not any other schemes? We need not apologise. The plain fact is that it is impossible to go much further by means of abstract schemes. We must revert to economic geography. The special problems of each sub-continent and country must be considered in turn.

41. I therefore propose that we should urge the Americans to agree to set up Joint Committees with us to report back on the main lines of future developments required in each region. This cannot be done in detail, of course, during the war. More profound study must be left to the World Resources Survey of Messrs. Hansen and Gulick. But rough approximations are possible. We want to get a preliminary sketch of the kind and scope of assistance which the Anglo-American Service may be able to give. Rough quantities are sufficient but we do want some quantities. Incidentally these Joint Committees would bring Anglo-American co-operation into being at once.

42. The committees must consist of men with first hand knowledge of the regions. They should be weighted in favour of those who have administrative and scientific interests against what may be called the prospector interest. The Anglo-American Service will be interested in welfare and ~~shun~~ exploitation. Each committee should have a pure economist and a pure statistician, who need know nothing of local needs, to keep an eye on the relevance of plans and projects to the general worldbalance and to the problems referred to in paragraph 18 of these notes.

43. The scheme for an Anglo-American board (Appendix III of the Memorandum) is largely a paper constitution and should be regarded as illustrative rather than definitive. It may be

considered in connexion with the proposals of Messrs. Hansen and Gulick. Paragraph 22 of the Memorandum refers to "severely practical difficulties". This is no doubt just; but we must eschew pessimism. For this is precisely the point on which we must show the greatest determination. Some institution of this kind is indispensable if we are to exercise a controlling influence on the balance of the world economy. And I have no doubt that if plans for economic surveillance fail plans for policing will fail too.

44. Besides a constitution, this appendix sets out three governing principles (pp. 79-80). For convenience I reproduce them here:

1. The British and Americans would wish to have scrupulous regard to aspects of welfare other than economic. In the case of primitive peoples care would be taken to avoid interfering with family, communal and religious practices and traditions. It would be no part of the plan to tear village communities up by the roots, to proletarianise vast masses of natives or create new and dangerous social problems among them. There must be no suspicion of exploitation. To safeguard the position the Board could set up an independent advisory tribunal of eminent men, regardless of nationality, who are recognised authorities on this type of anthropological subject, and publish its reports.

2. The Board would take a long view. For many years there has been a strong tendency towards national autarky. This has been due to some extent no doubt to motives of security, but also to the growing obstructions and uncertainties in international trade and to periodic depressions. The better success the Board had in maintaining the volume and balance of world trade, the less motive would countries have for seeking to obtain self-sufficiency.

Thus the Board would have regard to the most advantageous division of labour in the long run and not finance the development of industries inconsistent with that. For instance markets must be left for the export of manufactured goods from countries which cannot provide their own food and raw materials.

3. We do not yet know whether England and America will jointly or severally undertake the policing of world disarmament. This if taken seriously must have regard not only to finished weapons but also the types of industry readily capable of conversion for armament purposes and to the production of key materials in regions which cannot be fully relied on to pursue a peace-loving policy. Before approving any project the Board would consult the policing authority.

I suggest that each of these topics should be proposed by us for discussions with strong emphasis.

45. This discussion is bound to lead to the question how far, supposing that the greater part of world foreign investment is canalised through the Anglo-American Service, we can regulate development without seeming to domineer.

It is in the common interest that recent tendencies to autarky should be checked. These have largely been due to the fear and fact of war and to the fear and fact of trade depression. And it may well be hoped that in a more secure and orderly world the aspirations of peoples will turn in a healthier direction. But it will take time to re-establish confidence; there may be an awkward interlude. It might be wise to contemplate and even to define an interim period in which we shall play the governess rather more vigorously than we should plan to do when confidence and security were fully re-established. This is clearly an important matter for discussion.

46. My second principle concerns the international division of labour. This might well be the best place at which to project our anxiety concerning our balance of trade into the discussion. I hope that this may illustrate my contention regarding order and emphasis. Our main emphasis should be on the gravity and complexity of the world problem, which is a common cause of concernment to the two countries. We should devise a logical order for considering appropriate remedies. Some topics arising within this order are bound to be related to our private anxieties; then will be the opportunity to ventilate them; until then they should be suppressed.

47. When it does come round to our own case, we should be strong and insistent in our demands. The more self-restraint we show at the outset, the greater is the reserve of moral force with which we arm ourselves. We should go to these conversations as a potential joint victorious power, planning a pax Anglo-Saxonica and world prosperity, and not as a mendicant, hat in hand. Then, when a point arises touching ourselves, there will be an irresistible tendency to give us fair, yes, and generous terms. But, if we pay scant attention to the world problem and keep putting our difficulties in the forefront, we shall forfeit the respect that secures preferential treatment and belie the sense of responsibility that deserves it.

48. In paragraph 23 the Memorandum refers to the probability that the Americans will raise the question of nutritional policies. Nothing is said about our attitude. I believe that this is a most hopeful line of advance, and that we ought to be ready with proposals, or, at worst, counter-proposals.

49. Article VII refers to the expansion of consumption. Well, food is the most basic of all forms of consumption.

50. It will probably be agreed by both sides that if we are to have success in handling the problems referred to in Article VII and in paragraph 18 of these notes, pump-priming expenditure will be necessary. This is too often associated exclusively with capital construction; but there is danger of a surfeit of capital construction. I think it important that the advantage of directing pump-priming money straight into consumption should be recognised. I suggest that we should propose to link nutritional projects with the problem of pump-priming.

51. This also ties up most happily with our wish to check the trend to autarky and universal industrialisation, and to promote a healthy development among backward peoples.

52. It also has the advantage of having a breath of humanity. Banks, investment boards, buffer stocks are all extraordinarily impersonal. They also smack uncomfortably of pluto-democracy and international capitalism. Let us bring welfare into the picture. Let us think of the poor and under-nourished. And then let us think of cows and pigs. Let us tell the peasants of the world that we intend to help them to earn a better livelihood in occupations congenial to them.

53. The nutritional problem is one which must be tackled in detail by reference to the special problems of each locality. It should therefore be included in the terms of reference of the joint committees appointed to report on desirable developments by regions and countries.

54. It does not appear that our machine of government is altogether well adapted to handle the economic planning of the world. The Board of Trade and the Colonial Office can without doubt make contributions of great value. But we shall need some further organisation. The moment is inauspicious. Yet the issues are so vital, and the importance of our being as well documented and instructed as the Americans so great, that it may seem worth while to draw some few score people from our pool of man-power to form a planning bureau. The question of ministerial responsibility should also be considered.

55. I have heard the point put that in the period immediately after the war the prevailing maladies will not be depression, unemployment and poverty in the midst of plenty, but shortages of materials, shipping and man-power and a tendency to inflation. I accept the point and welcome it.

56. The post-war problems of relief, reconstruction and priorities should be tackled by the Anglo-American Service. These would provide tasks of a familiar kind. The immediate post-war economics will be of the same general nature as war

economics. There is advantage in the Service having for its first exercise a kind of work of which the technique is already known. By experience of co-operation in these comparatively straight forward tasks, it should gain strength and cohesion, and become a going concern, before it has to tackle the new and untried solutions of the long-range characteristic modern problems of unemployment and poverty in the midst of plenty.

57. This, however, is not a reason for not discussing the longer range problems now. For it is in regard to them that vital decisions and commitments have to be made, and the war-time solidarity of the two countries offers an opportunity for reaching agreement on these matters that may not recur.

58. To summarise, I propose

- (i) that the main text for the conversations should be the words in Article VII relating to the expansion of production, employment exchange and consumption, interpreted in the light of the typical modern problems set out in paragraph 18 of these notes;
- (ii) that to deal with these we should propose to establish a permanent Anglo-American Service, to full partnership in which Russia or other powers, could be admitted, as and when convenient;
- (iii) that Mr. Keynes' Clearing Union should be put forward and recommended primarily as the financial corner-stone of the Service;
- (iv) that it should also be recommended, as a means of dealing with the monetary side of the general problem and particularly with the relations between debtor and creditor countries; (there would be no need to refer to our own anxieties at this point);

(v) that the question of the Trade Cycle be raised for general discussion at an early stage, and that the buffer stock scheme be offered as the biggest single contribution which the Service could make to this problem by unilateral action; but that it be recognised that this should only be part of more far-reaching plans in regard to the Trade Cycle;

(vi) that the necessity be urged of having some such institution as an Investment Board for controlling the international flow of capital and thereby to some extent the direction of development in regions which need to import capital; and that the three principles set out in paragraph 44 above be brought prominently forward for discussion in this connection;

(vii) that under the heading of the second principle regarding the international division of labour the problem of maintaining export markets for countries which have to import the necessaries of life and raw materials be considered; and that the desirability of such expedients as the zoning of markets or agreed specialisation in certain types of export goods be considered.

(viii) that the need for preliminary realistic reports on the specific problems of sub-continent and countries and their most advantageous trend of development be urged; and that joint Anglo-American committees be appointed for this purpose;

(ix) that under the head of "expansion of consumption" we should urge the importance of the Service having a welfare side, not only for reasons of publicity but also as likely to promote healthy economic

developments; that nutrition might well be taken as the first branch of welfare to be dealt with; and that welfare schemes should be brought into relation with the problem of pump-priming expenditure;

(x) that the Anglo-American Service be instituted as soon as possible; and

(xi) that it be entrusted, by way of initiation, with the tasks of post-war relief and reconstruction.

59. I also raise the question whether some addition to our machine of government is needed to deal with these vast problems.

60. I put forward these notes with diffidence; I hope that they carry the ideas of the Memorandum a little further forward; I have at the same time the sense that they are still very tentative and preliminary, and that with further thought we should soon be able to introduce much greater clarity and order into our programme.

ANNEX I.

Control of Capital Movements.

I cannot feel entirely convinced that the proposal to control capital movements should be taken so early in the discussions. It appears to me to be too detailed and technical, anyhow if advanced on the grounds stated in the memorandum.

As a matter of proper order and emphasis I suggest that the question of capital movements ought in the first instance to be considered in the light of the observations set out in paragraph 44 of these notes.

The exploitation and deracination of backward peoples: the unhealthy trend to autarky: the creation of war potential among the less peace-loving peoples: these are great questions of policy in urgent need of discussion. If it be objected that capital seeks profit and therefore any tendency of foreign capital to develop countries on autarkic lines must be healthy and natural, the answer is of course that the profit may owe its existence to protection. Combines plant out their affiliates all over the world to avoid tariffs. Now it may be less difficult to curb this tendency by controlling the channels of foreign investment, anyhow initially, than to persuade countries to disrobe themselves of their protecting garb before they have had much time to experience the benefits of the new system.

It is to be considered whether we should hope to canalise a large part of foreign investment or even all of it through the Service, and whether any residuc proceeding privately should be licensed for the nature of the investment. This subject appears to be more fundamental than that of hot money and therefore due for prior discussion. When the greater question is settled it may be easier to decide the smaller one.

There are some *prima facie* objections to the proposal as presented. Would not the arguments in favour of it, which are set out in paragraphs 36-50 of the memorandum be largely superseded if the Clearing Union came into existence? Speculative movements could be approximately estimated, and their effects would be counteracted by the automatic accumulation of credits (and debits). The amounts transferred, could be subtracted from credit and debit accounts when these were to be used as criteria for the application of remedies to a lack of balance on current account.

Furthermore, will not the more stable conditions which we hope to see established after a certain lapse of time - and that controls must be retained for a certain period is not in question - remove the causes of the more vexatious movements?

May not this proposal savour rather strongly of the Schachtian way of thinking? And is it not in fact a relic of that? Will it be easy to persuade the Americans that it is possible to establish regulation of capital by the method of exchange control alone without having either to rest content with a very low level of efficiency or to enforce such an elaborate control as to jeopardise the multilateral system for current transactions by which they set so much store?

Finally is the proposal really in our own interest? The paper on the Balance of Trade provisionally estimates that we may have earned as much as £200 million by profit on these transactions in the period 1932-1938. Such a sum is not to be despised by a nation very anxious about her balance of payments.

I do not know by what virtue or cunning Englishmen succeeded in inflicting such losses on foreign speculators. Anyhow they were of help to their country. Is their enterprising spirit to be stamped out? Is every spark of initiative to be extinguished? Are we really bound to reduce ourselves to the bread and butter level of ordinary mortals? And why?

It is intelligible that the government of a poor country should wish to compel her citizens to husband their resources at home. But it is very paradoxical for the second richest country in the world to do so when her citizens have recently put their liberty to such good account. Why should we suspend against our own interest the law that to him that hath shall be given? Is this the manifestation of an unconscious suicidal instinct?

Why, even if it is decided to control investment in capital construction abroad for the larger reasons of policy, it might still be possible, and in that case surely also desirable, to leave Englishmen the means of earning some money by speculation in Wall Street at their discretion.

The case against speculative movements is the shock which they gave to exchanges, when these were subject to the somewhat precarious methods of control which were the best possible in pre-war conditions. With the Clearing Union all that will be altered.

I suggest that the proposal for exchange control of capital movements might well be adjourned.

ANNEX II.

Proposed Amendment to Clearing Union Plan.

The following note is intended to show that the bracketed alternative in paragraph 85(4)(C) should be made mandatory and would then become a dominant feature of the scheme.

The basic idea in the Clearing Union is simple and of vital importance. If a nation earns credit by exporting goods or services, she can only use it to import goods or lend. But hitherto if a nation had a tendency to earn more than she was disposed to spend in either of these two ways, in the process of adjustment she was apt to compel her neighbours to deflate or suffer their currencies to depreciate. Depreciation once begun was apt to be irregular and excessive.

The purpose of the Clearing Union is to alter the process of adjustment: to avoid deflation and secure that any currency depreciation is orderly and no greater than required to establish equilibrium.

In doing this it will throw into limelight and bring to the attention of nations the fact that credits earned by exports can only be used for imports or lending abroad. The credits will take the form of bancor accounts, which will only be usable for the purposes for which foreign currency is required.

If a nation does not import or lend sufficiently she will see that she is not using her credits. They will accumulate. Debits will also accumulate by an equal amount.

If the creditor nations will not use their credits for the only purposes for which they can be used, they will have no grounds for complaint. No blame will attach to the debtor countries.

Thus the onus of righting the balance is to some extent thrown onto the credit countries. If they do not choose to import or lend more, their money will stand idle, visibly idle.

So far so good. But without the proposed amendment the system would not be pushed to its logical conclusion and might soon fail to achieve its purpose altogether.

If we neglect the alternative offered in brackets, after credits (and thereby debits) have accumulated to a certain amount, pains and penalties begin to be inflicted on the debtor countries, not merely adjustments in their rates of exchange, which may be desirable because remedial, but more drastic measures.

Thus when this point is reached, the onus ceases to be on the credit countries. But why this? The larger the credits they accumulate, the more dog-in-the-mangerish they are being. Why take the onus off them as soon as they become sufficiently so? For a certain stage you tell them that they cannot have their cake and eat it. But if they accumulate a sufficiently big cake, do they become exempt from this law of nature?

Now there is a very good reason for imposing pains and penalties on debtors after a certain stage. It is to prevent any country or group of countries embarking on a rake's progress. The general level of debits depends on the degree of dog-in-the-mangerishness of credit countries; but the level of debit of a particular country may be due to its own uncontrolled and profligate habits. It may exploit the system to indulge in a career of razzle-dazzle. This must clearly be checked. Or it may be in a disastrous economic situation; this should indeed be remedied by positive measures but cannot be allowed to go on indefinitely at the cost of other people.

It is perfectly possible to combine the two objects of throwing the onus of using their credits onto credit countries and of keeping a check on debit countries whose position is radically unsound. The criterion for subjecting a debit country to pains and penalties should not be the size of its debit in relation to its quota (which we may call its index of debit) but the size of this index of debit compared with that of the debit countries generally.

Thus if the debits of all countries increased in step, no matter how much, the onus would still be on credit countries to right matters by buying or lending more; but if the index of debit of one country increased much more than the average that would be a signal for subjecting it to pains and penalties.

I understand that there is no objection to this proposal in principle and indeed the clause in brackets bears witness to this; but it would require a more complicated formula than those given in the text; and there is advantage in simplicity.

But this amendment is so crucial that we should introduce it at an early stage even at the price of a little complexity.

With the amendment, the plan provides a radical and permanent cure for the disturbance caused by credit countries that will not buy or lend. Without the amendment the plan may merely give a temporary breathing space. It may well happen that the debit countries generally will move more or less rapidly towards the point at which their overdraft facilities are exhausted and pains and penalties become imminent; they would then have to impose deflation in order to avoid the pains and penalties. In fact we should be back at the old state of affairs, the Clearing Union availing nothing.

Of course the size of permitted overdrafts could be progressively enlarged from time to time; but such revisions would undermine confidence in the system. It is much better to make it automatic from the beginning.

The following changes would suffice:-

Paragraph 85(4). Insert definitions:- The amount of a country's debit balance divided by its quota will be called its debit index. The amount of the debit balances of all countries divided by one half of the sum of quotas of all countries in the system will be called the world debit index.

(The one half comes in to allow for the fact that only some out of all countries will be in debit, the remainder being in credit).

The world debit index shows what may be called the average level of indebtedness at any time.

(a) line 2. Insert after quota "if this causes its debit index to increase by more than twice the increase in the world debit index." (This additional proviso will not apply to the second sentence).

(b) line 4. Insert after remedy "and if this increase of debit causes its debit index to increase by more than four times the increase in the world debit index".

(c) line 2. Insert in place of the words in brackets "and six times the world's debit index".