

THE ECONOMIES OF THE BRITISH COMPLEX

30 March 1955

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Mr. Martin Teall Flett, Financial Counsellor to the British Embassy, was born in Sutton, Surrey, on 30 July 1911. He spent his early life in Edinburgh, where he attended George Watson College. He returned to London in 1920 and completed his education at St. Paul's School and St. John's College, Oxford; is a Casberd Scholar of St. John's, and obtained a First Class in the Honor School of Modern History in 1933. Mr. Flett entered the Dominions Office in 1933, and in 1934 was transferred to H. M. Treasury, to which he has belonged ever since. During 1944-46, he was seconded for service in the Cabinet Secretariat, the Ministry of Reconstruction and the Office of the Lord President of the Council. He returned to the Treasury in 1946, and was promoted to Under Secretary in January 1949. In October 1953 he came to Washington as Deputy Head of the United Kingdom Treasury and Supply Delegation, Alternate Executive Director of the International Bank for Reconstruction and Development, and Financial Counsellor to H. M. Embassy. This is his first lecture at the Industrial College.

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30 March 1955

GENERAL NIBLO: Gentlemen: Our lecture this morning is on "The Economies of the British Complex." You realize that the economic potential of the British complex of nations is an important fact that must be considered when you evaluate the combined economic potential of the free nations of the world to wage war.

Our speaker's education and background, as well as his present position as Financial Counsellor to the British Embassy here in Washington and his position as British Alternate Director on the Board of the International Bank for Reconstruction and Development, particularly qualify him to discuss this subject.

It is a pleasure for me to welcome Mr. Martin T. Flett to this platform and to present him to you. Mr. Flett.

MR. FLETT: General Niblo, ladies, and gentlemen: My presence here today reminds me of the story of Mr. Albert E. Hicks which I found in a recent issue of the "New Yorker." Mr. Hicks was apparently a notorious pirate. He was finally caught and in 1860 was sentenced to expiate his crimes on a scaffold on Ellis Island in New York Harbor. Mr. Hicks was accompanied on his way to the execution by a distinguished body of gamblers, prizefighters, and politicians. During the trip a good time was had by all except, presumably, by Mr. Hicks himself. When the time came for him to mount the scaffold, Mr. Hicks was asked by the United States marshal in charge of the execution whether he wanted to make a speech. Mr. Hicks, a taciturn man, replied in the negative, whereupon the marshal exclaimed, "Oh, go ahead and talk. Make a speech. All the boys are expecting one."

I know that long experience of listening to lectures of all nationalities on a vast range of subjects has made you a thoroughly experienced and critical audience. Having spent my career in the British Treasury Department, I fear that I have perforce acquired that official taciturnity of all treasuries whose oratory tends to be confined to repeating the word "No" on all possible occasions. I must therefore begin by asking you to bear with me on a subject which cannot hope to rival the story Mr. Hicks could have told had he wished. Remember, like Mr. Hicks' audience, you asked for it, boys!

My subject today is "The Economies of the British Complex," and I am afraid that my task has not been rendered any easier by the definition of that complex which has been given to me.

In Britain we talk about the British Commonwealth, which has a population of 600 million people and embraces one-fourth of the world's total population. Our economists and administrators also talk a lot about the "sterling area," which has roughly the same population, but is made up differently because it does not include Canada, and does include a number of non-Commonwealth countries, such as Burma, Iraq, and Jordan. My terms of reference today, however, confine me to the British Isles, Australia, New Zealand, South Africa, and the British colonial possessions. I will do my best to keep within this definition, but I warn you that at times I will find irresistible the temptation to stray outside it into the wider Commonwealth and the sterling area.

The governing word in my terms of reference is "complex," which Webster's dictionary describes as "a whole made up of complicated or interrelated parts." I should like to begin by giving you a very brief description of the economies of the various parts that make up the whole of the British complex, and then to go on to describe the interrelation between these parts and some of the effects which flow from it.

The complex as a whole has a population of about 170 million people. Rather over 50 million of these people live in the British Isles, 24 million live in the other wholly independent countries of the Commonwealth, and 78 million live in the British dependencies. Geographically, the complex stretches eastward from British Honduras in the Caribbean to Pacific islands within a thousand miles of the coast of South America. Southward it stretches from the north of Scotland to the Antarctic. It includes within its boundaries every known variety of climate and temperature, and produces in some measure every major agricultural and mineral product, with the possible exception of some metals, of which nickel is one example and molybdenum is another. In 1953 the complex, as defined, produced 56 percent of the world's supply of wool; 41 percent of its tin; 25 percent of its copper; 50 percent of its cocoa; and 38 percent of its rubber. All of the countries of the complex use sterling, the currency of the United Kingdom, as their medium of international payments. Together with the countries of the Indian subcontinent and the non-Commonwealth countries to which I have referred, they make up the sterling area, which is the most important economic aggregation in the free world outside the United States.

Now, I shall turn to the individual countries and take as the first the United Kingdom which is, and always has been, the center of the Commonwealth. It has a range of industrial production as wide as that of the United States, although we do not pretend to compete with you in volume of output. Looking at the United Kingdom's economic potential objectively, and I will try to do it objectively, I think I would summarize its main merits as follows:

In the first place, as I say, it has the largest industrial potential in the free world, outside the United States. Its gross national product in 1952 was roughly two-elevenths of that of the United States; it was one-third greater than that of Western Germany; and it was 40 percent greater than that of France. In the field of defense, Britain is, I think, the only country in the world, apart from the United States and Soviet Russia, which is capable, in modern times, of equipping its own armed forces from its own industry.

The second source of economic strength in the United Kingdom is its highly skilled and well-educated population. Enjoying practically no raw-material resources except coal, the British people throughout history have had to live by their wits. The fact that we have survived so long and that our standard of living is still one of the highest in the world can in large measure be attributed to our success in keeping those wits sharpened. This technical achievement is not confined to the labor force, which has produced the Rolls Royce engine and has brought the yield of wheat, oats, and barley from an English acre up to roughly twice that of an acre in the United States. It is also seen, for instance, in the city of London, which has, over the centuries, developed that series of unique institutions and practices which make it even today the financial center of the world. I refer to such things as the British insurance companies, Lloyds of London, the international banking system, and the many commodity markets through which the produce of the free world reaches the consumer. The importance of London in this respect can be illustrated by the fact that when we reopened the London gold market in 1953, after it had been closed since the outbreak of the war, it immediately attracted back to it the vast majority of the free world's gold output.

I would suggest that the third outstanding virtue of the British economy is its technological achievement. This is only another way of saying the British people still live by their wits. But the list of things in which the British have pioneered development is, I suggest to you, very impressive. To take a few instances: In 1936, we had

the first public television service in the world. Whether that is an advantage or not, I leave to you. In 1941 we put into the air the first practical gas-turbine aircraft. Our world lead in the development of radar was one of the determining factors in the Battle of Britain. British scientists were largely responsible for the discovery of vitamins and penicillin. Dacron is a British invention, although we call it Torylene in England. We have just announced a program for the construction of nuclear powerplants which by 1965 will meet a substantial proportion of our total electricity requirements.

Against these elements of strength in the British economy must be set a number of weaknesses. In the first place, our population is aging. At the last national census, no less than 11 percent of the British people were over 65 years of age, as compared with an estimate of 8 percent for the United States. I gather that the experts reckon that in 20 years' time the British figure will have risen from 11 to 16 percent, while the American figure will have risen only from 8 to 11 percent.

In the second place, owing to the size of our population and our lack of indigenous raw materials, the United Kingdom is peculiarly dependent for its livelihood on imports and exports. This, of course, has one incidental advantage, as it has brought into existence the largest merchant navy in the world. But it is certainly an embarrassment in war. Indeed, from our point of view, there is no question whatever that the Battle of the Atlantic was the crucial battle of the Second World War.

The third disadvantage, certainly, compared to the United States, is the vulnerability of our economy to enemy attack in wartime. If I did not mention this factor, which is so paramount in our minds today, I could not pretend to be giving you the full picture. Having mentioned it, however, I should say at once that I personally am completely unqualified to discuss either the extent of that vulnerability or the means by which it can be mitigated. I hope you don't ask me any questions on that one.

These, as I see them, are some of the outstanding characteristics of the British economy. I hope I have been objective. To make the picture complete, however, I must say something about its present state of health. I think it is difficult for an American to appreciate the strain which World War II placed upon the United Kingdom. Despite the enormous, indeed, and perhaps the decisive, assistance which we

received from your generous lease-lend policy, these six years of war transformed Britain from the world's largest creditor nation into the world's largest debtor. Perhaps even more serious was the fact that we emerged from the war with exports only one-third of the pre-war level, and that the industrial base upon which we had to depend to recapture our export markets had been seriously damaged by enemy action and worn out by the war effort. Moreover, during the war, the so-called terms of trade had moved against us. The price of raw materials which we had to import had risen more sharply than had those of the manufactured goods which we had to offer to our customers. Henceforth we were going to have to exert a greater proportionate effort to secure the same volume of imports.

Britain's economic history since 1946 consists largely of a concentrated effort to regain the ground that we had lost. By 1953 we had gone a very long way toward achieving this objective. Our balance of payments was reasonably satisfactory; the restoration of our industry to its prewar efficiency had been largely achieved--although of course we had lost the 10 years of growth that we would have enjoyed in the absence of war--and our exports were 50 percent higher in volume than they had been in 1938.

It cannot, however, be said that we are yet out of the wood. Despite the increase in the volume of our exports--as I said, they were up by 50 percent in volume--we could still in 1953 afford to buy only about 85 percent of our 1938 level of imports. Moreover, the whole of our economic policy has been bedeviled by the weakness of our reserves of gold and dollars. These reserves, which are the reserves of the entire sterling area, are of crucial importance to us, as they are the ultimate means by which we can cover the gap between the payments that we have to make for our essential imports from the "dollar area" and the gold and dollars that we can earn by our export of goods and services.

In 1953 they represented no more than a 2-month turnover of the total trade of the sterling area, whereas I understand the comparable figure for the United States reserves was over two years. Indeed, it cannot be said that the United Kingdom has finally regained its economic health until we have reached the point at which sterling can become and remain fully convertible with the United States dollar. British policy is striving hard to attain this objective, but its achievement must depend on a number of factors, not the least, if I may say so, upon the foreign economic policy of the United States.

I now turn to the second component of the British complex, which consists of the independent countries of Australia, New Zealand, and South Africa. To these I would add, for the sake of convenience, the new Federation of Rhodesia and Nyasaland, which is very near to full independence and whose economy exhibits many of the same characteristics. All these countries have their own individual features and problems. This morning I can only attempt very briefly to set before you some important characteristics common to them all.

The first and most obvious of these is the extent to which all these countries are dependent upon primary production for their living. Take the case of New Zealand--in 1953, 36 percent of her export earnings came from wool, 22 percent from butter, 18 percent from meat, and the entire balance from other products of the farm and field. Or take South Africa, who in the same year derived over one-third of her total foreign earnings from the products of her gold mines, and a further one-sixth from her wool production.

The second notable feature of these countries is that they are all expanding their economies very rapidly. The European, which is the largest immigrant population of Southern Rhodesia, multiplied two and a half times between 1938 and 1952. Australia in recent years has been accepting immigrants at a higher rate in proportion to her total population than was ever achieved in the United States during the peak inflow of European immigrants during the nineteenth century. In eight years Australia's population has risen by 20 percent.

From this factor flows the consequence that all these countries are short of capital with which to finance their development, and must constantly borrow new resources from the capital exporting countries of the world. Fortunately for them, they can offer to investors the attractions of stable, honest internal government, an unblemished credit reputation, and sound economic prospects. It is for reasons like these that Australia is now the largest single debtor of the International Bank, and has recently been able to raise her first postwar loan, on her own credit, in the New York market. Nevertheless, the urge to expand has, since the war, at times outrun the resources available for the purpose, and all these countries have in the past 10 years experienced occasional embarrassing bouts with inflation.

The third common characteristic of these countries is their growing industrialization. Compared to their primary production, the figures for industry may not be particularly impressive. But, if we are talking

of war potential, we should take note that in 1954 Australia produced nearly 2.5 million short tons of steel and over 60,000 motor cars of its own design, and that South Africa's industrial output increased by 60 percent between 1943 and 1948.

The third component of the British complex is the British Colonial Empire.

Here perhaps I may digress a moment to say something about the place of the colonies in the Commonwealth. I know well that ever since 1776 "colony" has ranked as rather a dirty word in this country, and Englishmen who are foolhardy enough to call an Australian or a Canadian a "colonial" do so at their peril. Nevertheless, I do not think that the modern Commonwealth has any reason whatever to hang its head in shame on the subject of the colonial Empire. Constitutionally, Britain has honestly striven for many decades to bring its colonial territories to the point at which they are ready to exercise complete sovereignty, and I can assure you that the political representatives of the colonies themselves take good care to see that the point at which this stage in their development has been reached is not left to the unilateral decision of the bureaucrats of Whitehall.

Economically, the colonies benefit in several ways from their status in the Commonwealth. Many of their exports enjoy a substantial preference in the United Kingdom and, in the case of some commodities, such as sugar, this amounts to a guaranteed market. A large proportion of the cost of their military protection which, as can be seen by the cases of Malaya and Kenya, can be very high indeed, is borne by the United Kingdom. Moreover, despite the strain imposed upon her own resources by the task of recovering from the war, the United Kingdom is this year providing her colonies with over 150 million dollars in grants alone, and a much larger amount in loan capital.

I know that it is often said that economic benefits are no compensation for colonial status, and Patrick Henry's war cry has echoed around the world. But I would ask you to remember that Ceylon, the last country in the Commonwealth to achieve full independence, has remained within it of her own free will, and that the Prime Minister of the Gold Coast (which will in all probability be the next country to cross the frontier to independence, and is expected to do so within the next two years) has already announced his intention of seeking to follow Ceylon's example. I might add that in Malta, a colony which already enjoys complete independence in her internal affairs, and which is probably

well known to some of you gentlemen, there is even some talk of seeking complete absorption into the United Kingdom and becoming another part of it, like England, Scotland, Northern Ireland, and Wales.

I am afraid that it is quite impossible for me to describe in any detail the enormously varied economic circumstances of these territories. They range from the highly industrialized city of Hong Kong to the most primitive subsistence economies in Africa. It can, however, be said that, broadly speaking, they show all the characteristics of underdeveloped countries throughout the world. There is the dangerous dependence on one or two primary crops. No less than eight colonies derive more than 70 percent of their export earnings from a single export. (Curiously enough, in the case of Zanzibar, this crop happens to be cloves.) There is the consequent vulnerability of the economy to world price movements outside the colonies' control. There is the urgent need for the basic services of transport, power, irrigation, sanitation, and education, without which no significant increase in the standard of living is possible. And, finally, there is the lack of skilled manpower which places an overriding limitation on the pace of economic progress. In this latter respect the colonies, broadly speaking, differ from the independent countries of the Commonwealth. The brake on development in the colonies is trained manpower. In the independent countries it is material resources.

So far, I have been speaking separately of what Webster calls the "complicated and interrelated parts" of the British complex. What are the additional elements of strength that the complex derives from the fact that these parts make up a whole?

This, I think, can be aptly summed up in Webster's definition of the other form of complex--the psychological one. He described this as "a system of desires and memories which . . . exerts a dominating influence on the personality."

The British complex--and here I am afraid that I must speak of the Commonwealth as a whole--is bound together by factors which have in the past, and will I hope in the future add greatly to the sum total of the strength of its individual parts.

The first influence is the common respect for a constitutional tradition of ordered freedom and parliamentary government which was English in origin but has, in the course of the last 200 years, been greatly enriched by contributions from elsewhere in the Commonwealth. The lesson of freedom which your original settlers brought with them

from England, and had to reteach to the mother country at Yorktown, has been well "learnt." The whole constitutional history of the second British Empire can be regarded as a progress toward self-government by its component parts. Today the Commonwealth has often been described as a procession headed by its eight independent nations and stretching backward through a bewildering variety of constitutions representing practically every stage of the advance of self-government.

It has, moreover, been a singularly fortunate feature of the Commonwealth's development that the growing political independence of its members, one from the other, has not affected the ties of respect and sentiment which bind them together. It is a curious feature of the Commonwealth that it has no central organs of any sort except the British monarchy. Even here, the Queen reigns in Canada and Ceylon as Queen of those countries and not as Queen of the United Kingdom. She does not, in fact, reign in the Republic of India at all. Her position there is solely that of "Head of the Commonwealth."

The machinery which keeps the Commonwealth together is in fact the machinery of joint consultation between independent sovereign nations. This goes on continuously on all levels and on all subjects. There are Prime Ministers' conferences, Foreign Ministers' conferences, conferences of the speakers of the different parliaments. There are even conferences of the governing authorities of the game of cricket, which is itself no mean cement in the Commonwealth structure. Through such consultations the Commonwealth strives to attain the widest measure of agreement on the problems which face it. Naturally, such agreement is not always complete between countries whose circumstances are so different. But Commonwealth conferences tend to be more successful than most international gatherings in hammering out a common line of policy and, once this has been achieved, the strength of mutual respect and understanding within the Commonwealth helps to insure that each independent member country makes its full contribution towards carrying that policy into effect.

It is with one of the most important of these arrangements for Commonwealth consultation that I am particularly concerned today. The periodic economic conferences of Commonwealth Finance Ministers are in effect the coordinating element in a system whose purpose is to give the strength of unity to the individual members of the club. They are the apex of a pyramid of constant economic consultation at all levels, both formal and informal. Let me at once say that there is in this system no more unity in the sense of unified control

or direction than there is unity in the direction of the foreign policies of say India and Pakistan and Canada. Here again the Commonwealth functions by discussion between equal partners and seeks to achieve unity of purpose in the mundane task of thrashing out the wording of a joint communique. Nevertheless, there is a system, whether we are prepared to admit it or not--the system which has come to be called the sterling area.

I do not think that it is necessary for me to attempt to give you a detailed account of the history and workings of the sterling area. Fundamentally, it is the material expression of the fact that the economies of a large number of countries throughout the world are so closely connected with that of the United Kingdom that they have based their own currencies on sterling, use sterling in their international transactions, and hold a substantial part of their own reserves in that currency. It is for this reason, incidentally, that Canada, whose economy is so closely integrated with the United States, is not a member of the sterling area. It is also for this reason that a number of non-Commonwealth countries, like the Irish Republic and Burma, remain in it. It does cover, however, the whole British complex as it has been defined for me today.

How does the existence of the sterling area increase the strength of its component parts? I suggest that it does so in three ways.

In the first place, its most outstanding feature is that it pools its reserves of gold and dollars. This means that whatever happens to the terms of trade, it can maximize its trade with those areas in the world, notably the United States and Canada, which demand gold or dollars for their exports. If these reserves were split up among the individual countries and each of them had to conduct its trade in such a way as not to let its own little hoard fall below the danger line, there would be much less trade. Every country in the area, moreover, benefits from the fact that it embraces both industrial and primary economies, because this means that whichever way the terms of trade may swing there will always be some part of the area contributing to the central pool.

In the second place, trade flows more freely within the sterling area than within any other group of countries in the world. This is partly due to the fact that the area consists of countries whose economies have always been complementary--the United Kingdom supplying the manufactured goods and the outer sterling area supplying the primary

products. But it is also due to the fact that all parts of the area trade and keep their accounts in the same currency.

Thirdly, and for similar reasons, there are very few impediments to the flow of capital within the sterling area. The world is beset by exchange controls. An Englishman cannot transfer his capital to the United States without a government permit, which, I can assure you, the British Treasury makes hard to obtain. Many countries even limit the remittance of current earnings to a foreigner. None of this happens in the sterling area. The freedom of capital movement inside the sterling area is therefore of great importance to capital-hungry countries like Australia and New Zealand.

Of course ties of kinship, mutual understanding, unhappy experiences of investments in foreign countries, and many other factors naturally tend to attract British capital to other countries of the Commonwealth. But the ease with which capital can be moved within the sterling area has greatly accentuated this movement and has contributed substantially to the rapid economic development of its members since World War II.

I think therefore that I can sum up the economic value of the British complex to its members by saying that, first, it gives to each and all of them a vital interest in the economic health and the strength of the others; second, that this interest is fostered through constant consultation which insures that experiences are pooled, and every country in the area knows and appreciates the problems of its fellows; third, members of the club try, so far as possible, to make their economic policy consistent with its general objectives; fourth, by membership of the sterling area, countries on its circumference benefit substantially so far as their needs for capital resources are concerned; and, finally, if any member of the area gets into serious difficulties, it is a matter of self-interest to the other members to see that she gets out of them as effectively and expeditiously as possible. In fact, every country in the sterling area knows we have to sink or swim together.

So much for the structure and interrelationship of the British economic complex. What of its future? This depends partly on its own conduct of its affairs, but partly also on what happens in the outside world, and particularly in the United States. Fundamentally, the countries of the sterling area are already strong and their undeveloped resources are enormous. But I would not pretend that their combined economic strength, let alone their individual strengths, can hope to rival that of the United States within the foreseeable future.

To take just one figure, the British steel production capacity is the third largest in the world. We are very proud of the fact that it amounts to over 20 million tons a year. I believe the last figure I saw for the United States steel capacity was 125 million tons. We of the sterling area, therefore, are acutely conscious that we cannot hope to achieve and retain full prosperity entirely by our own exertions. For this we must look to the cooperation of the United States and the rest of the free world. Of course, our first duty must be to keep our own house in order. There have been times since the war when it seemed rather untidy. We had the excuse that the war had made a mess of it, and that we were not strong enough to put it in order very quickly. Indeed our anxiety to go ahead faster than our resources allowed was one of the many factors leading to the three serious balance-of-payments crises of 1947, 1949, and 1951. But I think that we can reasonably claim that by the time we had survived the last crisis we had learned our lesson. This lesson was spelled out for us at a very important economic conference of Commonwealth Prime Ministers in December 1952, and consisted of two parts:

1. A country which is suffering from internal inflation cannot hope to maintain a satisfactory external balance of payments. All members of the sterling area must therefore live within their means if its vital reserves of gold and dollars are not to disappear down the drain of trade deficits.

2. Every effort must be made to develop as rapidly as possible the latent resources of the area.

We were promised by our Prime Ministers on that occasion that, if we showed by our actions that we had taken this lesson to heart, we would be within sight of the day when irksome exchange restrictions could be removed and our period of postwar convalescence brought to an end. It is the lesson that we have been trying to apply ever since.

On the whole, I think that we have been reasonably successful. Since the 1951 crisis we have managed to add one billion dollars to the central gold reserves of the sterling area, and this despite the recent slight recession in your own economy. This was quite an achievement, as our failure to weather your 1949 recession cost us so many dollars that we had to devalue sterling. Meanwhile, we have continued to pour money into the development of our economies both in the United Kingdom and overseas, with the result that they are today very much stronger than they have been at any time since the war. In this connection I might say that, despite our loss of resources during the war,

the United Kingdom has continued to export capital on a very much larger scale, proportionately, than the United States. During the period 1946 to 1953 our net export of capital (very largely to the Commonwealth) was estimated at 120 million pounds per annum.

It is true, of course, that in the last few weeks signs of incipient inflation have reappeared in the economies of both Britain and Australia. Both countries have had to take steps to curb an undesirable drain on their balance of payments. But the rapidity and the severity with which both governments acted is, I think, in itself a reassuring sign that they have learned their lesson and are determined to put it into effect.

I am not attempting to claim for the sterling area any undue degree of virtue for taking what harsh experience has taught it to be the only sensible course. What is much more relevant is that no amount of native virtue can restore the area to full prosperity without the cooperation of the outside world. International trade is the life blood of the sterling countries, all of whom are many times more dependent on imports and exports than the United States. The 1952 Commonwealth conference therefore set on foot the so-called "collective approach to freer trade and payments." This was designed to reestablish the free exchange of currencies by making the pound sterling freely convertible and, by doing so, to open the way to the exchange of goods and services throughout the world, without the artificial barriers of exchange controls and import quotas.

The fundamental conditions for such a step were seen to be prudent management on the part of the sterling countries, and some assurances from the outside world that, if the sterling countries did behave themselves, they could rely on earning a sufficiency of foreign exchange to enable them to keep sterling convertible.

I have referred before to the fact that the central reserves represent only a 2-month turnover of sterling area trade. The 64-dollar question of convertibility is whether we can keep this pot sufficiently full to give to anyone holding sterling the confidence that he can draw dollars against it if he wants to do so. If he hasn't got that confidence and feels that the dollar is a safer currency for him to hold than sterling, he would be silly not to seek to convert as soon as he is allowed to do so. This will cause a run on our bank, and we shall have to close our doors.

It is here that the role of the United States becomes of such crucial importance. You are the only great creditor country left in the world. If other countries demanded gold from us under the conditions I am envisaging, we could hope to get it back from them in trade settlements, either directly or indirectly. But there is so much that we must buy from you, and so much more that we would like to buy from you if trade and finance were freed from their present restrictions, that convertibility will always hold great risks for us until we can see our way to balancing our accounts with the United States. I know that the recent rise in our gold reserves, for which I have just sought to take credit, is largely due to the flow of United States dollars into the rest of the world in the form of economic aid and extraordinary military expenditure. The world is not perhaps always as grateful as it should be for these dollars. But I must point out that aid and extraordinary overseas expenditure are a very insecure basis for sterling convertibility. Aid, like charity, can always be cut off at the discretion of the donor. Military expenditures may fall. Indeed, the combined efforts of our nations' foreign policies are directed to securing that some day, some time, they should fall. What we in the sterling area, and in the whole world outside your boundaries, are seeking is a reasonable assurance that, provided we make the effort in free and fair competition, we can earn on our own merits the dollars that we need to balance our accounts with you. We are only too anxious to make that effort. But you must allow us into your markets if we are to do so.

In the period 1946-54, the sterling area spent 25 billion dollars in the United States, and earned only 20 billion dollars with which to pay for it. In other words, with our hatches battened down and our purchases from the "dollar area" restricted to absolute essentials, we were still 5 billion dollars in the red.

It is for this reason that we are watching so anxiously the fate of American economic policy.

COLONEL BARRETT: Gentlemen, Mr. Flett is ready for your questions.

QUESTION: Sir, what is the status of Hong Kong in the Commonwealth? What are its assets, and how big are they?

MR. FLETT: Are they all going to be as difficult as this? The population of Hong Kong is 2.3 million. Its status is that of a crown colony. This means that it enjoys a large measure of independence in

the administration of its internal policy, but that its foreign policy is subject to the control of the British Government. Its historic importance is that it has been one of the main ports by which world trade flows into China, and although its direct trade with the Chinese mainland has diminished, it remains one of the most important entrepots in the Far East.

QUESTION: Sir, could you comment on the potential amount of population that Australia could support, and what are the limiting factors?

MR. FLETT: I have no idea what their potential is. I think their present population is 9 million, and the potential might be at least double that.

The main limiting factor, as I see it, is probably water. The center of Australia is a vast arid desert, which has not so far shown many other resources to compensate for lack of water. I think that this is one of the reasons for the difference between Australia and Canada. With the development of the new technique of mapping and exploration by air, Canada has found herself one of the richest countries in the world. The Australians, on the other hand, have found in their central desert little except the deposits of uranium at Rum Jungle. The population of Australia therefore looks like having to continue to cling around the rim of the continent.

Another limiting factor on population, I suppose, is the comparative inability of Europeans to settle in the tropical north, and the Australian reluctance to admit Asiatic immigrants.

QUESTION: Going back to Hong Kong for a moment, in discussing the recognition of Red China, would you like to discuss the trade of nonstrategic materials with China and the extent at which such trade might overthrow the enterprise for controlling strategic material?

MR. FLETT: Not particularly, but I will have a shot at it if you like. I think this is one of the points on which there is some difference between the British and the American approach. So far as strategic materials are concerned, there is complete agreement, as I understand it. The two countries got together and decided on the list of strategic materials and are bound by that agreement. We believe, however, that there is some advantage in trading with Communist China in nonstrategic materials. I think that we regard ourselves as clever enough to secure from such trading at least as much benefit for the Western World as we confer on the Chinese.

QUESTION: What have been the results of your recognition of Red China, economically? Have any of your businessmen got a pound or a farthing out of their investments in Red China?

MR. FLETT: I don't think the Red Chinese are treating us any better than they are treating your businessmen. Although I have no figures, I do not believe that, in fact, very much trade is passing. China has not very much to offer in the world. In so far as we are trading with China, however, we are getting paid. But generally speaking our investments in Red China have been treated no better than yours.

QUESTION: Mr. Flett, would you explain the difference for me between the sterling area and the sterling bloc?

MR. FLETT: The sterling bloc was in effect the name applied to the present sterling area during the thirties. At that time the sterling bloc consisted of roughly the present sterling area plus a number of other countries such as Egypt and Palestine, and, I think, the Scandinavian countries. Then came the war and the imposition of exchange control by the British authorities and the other belligerent members of the area. The sterling area today is the area around which exchange-control fence was erected at the outbreak of war. In other words the sterling area is the modern version of the sterling bloc.

QUESTION: Mr. Flett, I infer from one of your last statements that you are interested in what our economic policy will be. I suppose you are referring to the possible changes in our tariff act and in our trade policy with relation to the world. What are the British tariff policies? Are there any tariffs between the countries of the sterling area? Are there any between the Commonwealth areas which are outside the sterling area, such as Canada? What in general, then, is the tariff situation in the British Commonwealth or the British complex?

MR. FLETT: My impression is that, within the sterling area, and indeed in the world as a whole, outside the dollar area, tariffs are not at the moment terribly important as barriers to trade. As you probably know, the main means by which nondollar countries are protecting their economies is the imposition of import quotas. In other words I think that very few American exports to the United Kingdom have been frustrated by the British tariff. What has frustrated them has been the British system of import quotas. As regards general tariff policy, we have in Britain a low tariff wall. This sometimes

strikes the outsider as being considerably higher than it is, because of the existence of a British purchase tax. If an Englishman wants to buy a British motor car, something like one-third of the cost he pays represents purchase tax. Anyone bringing anything into the British market has to pay this purchase tax in addition to the tariff charges. The salesman, therefore, who lands his car on the docks in England is faced with a demand for something like 30 percent of its value and sometimes mistakes the purchase tax which his British competitors are also paying for an iniquitous protectionist tariff.

The independent countries of the sterling area conduct their own tariff policies without outside interference. On the whole their tariffs are higher than ours, and of course are designed to protect their own economies.

There is an arrangement called imperial preference under which, in respect of some commodities, countries of the Commonwealth give one another a slight edge in tariff rates over the outside world. The scope of this scheme has been considerably reduced since the early thirties, and I do not think that, broadly speaking, it can be extended again. As regards the dollar countries and the nondollar countries, there is no difference in tariff rates in the sterling area. In other words our tariff on French motor cars is the same as our tariff on American motor cars.

QUESTION: In the discussion about the economic potential of Africa and your administration in South Africa, we more or less have the impression that the potential of the Central African region, having in mind Nigeria, the Gold Coast, Kenya, and so on, is rather in the dim future. It looks to us as if, with natives with such a low level of education, communication, and transport, it will be a matter of centuries before you can hope to get any substantial contribution to the free world out of it.

MR. FLETT: I would not say centuries. This is a thing I referred to in my talk--the development of basic resources. As long as you can put in your roads, highways, power, irrigation, and that sort of thing (and this is a thing which has to be done by the government because, generally speaking, it is not a thing which will attract private investors) economic development can be very rapid. In the Central African Federation for instance which consists of Southern Rhodesia, Northern Rhodesia, and Nyasaland, this potential is already very great. They produce 25 percent of the free-world copper and are going ahead very

fast indeed. I should say the economic potential of the free world will be greatly strengthened by Central Africa within a decade.

QUESTION: Would you please discuss the competition that will be given the United Kingdom industries and economy by Japan and Germany?

MR. FLETT: Oh, well, I can't assess it. Obviously it is going to be very stringent. Germany and Japan, roughly, produce and want to export the same type of things as we do and you do. All I can say is, that if we don't maintain our export trade we die. The suicide rate in the United Kingdom has never been very high.

COLONEL WIRAK: Sir, I wonder if you would give us the fate of the very important coal industry as of 1965 when your atomic plants get into production?

MR. FLETT: I don't have the exact figures, but I think that the atomic energy we hope to produce by 1965 is something like the equivalent of 6 to 10 million tons of coal per annum. Our total coal output is, at present, something over 200 million tons a year, so I think that the whole of this nuclear power production will be taken up in the increase in consumption during the period.

QUESTION: Can you explain why the British Government in its own country maintains high taxes on motor cars and gasoline as opposed to greater development of those industries if the taxes on cars and gasoline were considerably lower, which would result in possible expansion of all the connected industries along with them?

MR. FLETT: I fear that all our taxes are high. The high taxes on the motor car industry and on the gasoline industry have however an economic justification. Our motor cars are probably one of our most important exports of manufactured goods and taxation at home helps to make cars available for the export market. On gasoline, broadly speaking, every ton we import costs us dollars. Therefore we want to restrict the consumption of gasoline and push out the export of motor cars.

QUESTION: In order to develop natural resources, Canada needs migration and capital. I believe that a reasonable number of British people would like to emigrate, but the roadblock is convertibility of currency. Is there any alternative solution to this mutual problem?

MR. FLETT: I don't think the roadblock is really convertibility of currency. I quite admit it is more difficult for an Englishman to go to Canada than to Australia. I think one of the main difficulties is that there are not enough of us. I mean that on this question of emigration from the center of the circumference, you can produce a good argument saying we ought to scatter our population from the United Kingdom because our islands are overpopulated. You can also produce a good argument saying we have not enough people in the United Kingdom. The Englishman who wants to emigrate can go to Australia, Rhodesia, and so forth. All those countries are crying for them.

While it is difficult to answer a hypothetical question with confidence, I doubt whether, if we open the gates wider to Canada, there would be a very great increase in emigration. I don't know. I should add however that we realize the desirability of removing such barriers to emigration to Canada. For this reason we did, in fact, ease our exchange restrictions on immigrants to Canada last autumn.

QUESTION: You said that for every ton of petroleum you imported it cost you dollars. I think you said Iraq was in the sterling area.

MR. FLETT: What I mean is that while we have the second largest petroleum industry in the world, oil is very much a dollar commodity. You can always get either dollars or dollar worth for the export of your oil. If you consume your own oil in pleasure driving, you have to that extent deprived yourself of the chance of earning or saving dollars.

QUESTION: Sir, you have made the statement that British agriculture was more productive than ours in wheat and other grains. Would you comment on that and tell us why there is greater productivity in the United Kingdom?

MR. FLETT: I am no agriculturist. You can take anything with a grain of salt. I think, however, that the answer is that there is more intensive production. Our agriculture, which is very highly mechanized, is directed to harvesting the last possible grain from our small area of land. Perhaps also we have looked after our soil a bit better than you have. Helped a little by our wet climate, we haven't had a dust bowl as yet.

QUESTION: Regarding this export of British capital that is going on, is that pretty much freely directed, or is it government directed along lines intended to best increase the economic potential of the

Empire, or in combination with the United States in our joint economic potential increase?

MR. FLETT: It is both. In fact it is three things. In the first place, there is government directed capital going abroad. For instance, we have released 60 million pounds of our subscription to the World Bank--which is in sterling--and the World Bank can now lend this to any country in the sterling Commonwealth which has satisfied a number of criteria laid down by the British Government. In the second place, there is borrowing in the London market by the governments of individual sterling area countries, which is directed by those governments into the channels which they consider most necessary. Finally, there is the export of private capital by individuals and commercial companies. If you have capital available in the United Kingdom and you want to invest it in Australia, you can do so without securing the permission of any government organization.

QUESTION: Where would you place the petroleum industry in the rehabilitation of the British economy since the war--first, second, third, fourth, or where?

MR. FLETT: It has made an enormous contribution. After the war, when our resources were at an absolute minimum, we deliberately gave to the British petroleum industry all the resources that it needed for its development. From the point of view of our balance of payments the industry is at least one of the first six contributors to our recovery. It has been a very great dollar earner. You must remember that there are British oil interests in South America as well as in the Middle East.

COLONEL WALSH: Mr. Flett, you referred to both the sterling bloc and to the dollar area--Canada, being tied to the United States economy. To what extent are the sterling bloc countries tied, formally? Canada is tied to the United States informally. Are there meetings between the various countries of the sterling bloc to make agreements? Are they required?

MR. FLETT: I had hoped that I had dealt with this in my talk. There is no formal agreement between the sterling area countries. There are many agreements on individual subjects between individual countries. Britain, for instance, has agreements with India and Pakistan regulating the rate at which our wartime debt to these countries--their so-called sterling balances--is liquidated. But there are no formal agreements laying down how the sterling area should work.

COLONEL WALSH: The thought occurred to me, for instance, that a central American country, like Venezuela, say, in the dollar area, without any formal agreement at all, is under the influence of United States economy.

MR. FLETT: It is the same thing in the sterling area.

COLONEL WALSH: That is what I wanted to explore.

MR. FLETT: In the sterling area the main factor is the influence of the British economy. Venezuela for instance could hardly join the sterling area. Her balance of payments with the dollar and sterling areas is such that she has to demand dollars from the sterling area in order to meet her payments to North America. The so-called dollar area is, to a large extent, the concept of the sterling area, and I doubt whether your authorities would consider talking about it in the same way as we do. To us the dollar area is that part of the world to which we have to pay dollars because it will not accept sterling.

QUESTION: What is the debt of the United Kingdom and what is the gross national product, in dollars?

MR. FLETT: Will you tell me the gross national product of the United States?

STUDENT: About 365 billion dollars.

MR. FLETT: Well, I know our national product to your national product is as 100 to 550. It is two-elevenths of your gross national product. As regards our debt, do you mean our external debt or our internal debt? Is it what the British Government owes to the inhabitants of Britain because of their investments in government securities or is it the debt that Britain as a nation owes to other nations in the outside world?

I said that we have changed from the biggest creditor to the biggest debtor. Roughly speaking, we now owe the world something over 3 billion pounds. What we owe the British taxpayer I don't know. I think it is about 20 billion pounds.

COLONEL BARRETT: Mr. Flett, I know I speak on behalf of the Commandant, the students, and the staff and faculty when I tell you we are doubly appreciative of your splendid presentation and your courtesy in answering questions.

(19 May 1955--250)S/sgH