

This chapter is in one sense a continuation of the Appendix to the first chapter of Part II "Exchange Control". The graph shews holdings of the Exchange Equalisation Account since 1932.

At the outbreak of war total U.K. liquid assets were estimated\* at something over £1,000 million:

	<u>£ million</u>
Gold held by Monetary Authorities (excluding forward sales and other outstanding commitments)	479
U.S. and Canadian dollars held by Monetary Authorities	15
Other short term balances abroad	300
Securities* (said to be "fairly readily marketable")	
U.S.	220
Canadian	40
Sterling (possible sale)	<u>20</u>
	<u>280</u>
	<u>1,074</u>

against which were to be set liabilities<sup>†</sup> as follows:-

Overseas balances in London	445	
" holdings of British Government securities	<u>185</u>	630
Leaving a net <u>surplus</u> of, say		<u>450</u>

There were then £494 million immediately available to meet current and prospective expenditure in hard currencies; holdings of foreign currencies other than dollars were negligible.

The other

\*"Stamp" survey and H.M. Treasury. Later estimates put the securities at a higher value, perhaps as much as £100 mn. more.

† Of which Foreign balances in London	240	
" holdings of British Government Securities	<u>80</u>	
	320	
		<u>    </u>

The other assets had to be mobilised by the operation of the new Regulations, and if in the form of securities, vested in the Treasury and realised. Moreover, £49 million of the reserves was earmarked to cover net forward sales of gold and dollars.

Changes in the gold and currency holdings of the E.E. A/c. between 1932 and the outbreak of war, as we have seen, are conveniently regarded as falling into *four* periods, and were influenced predominantly by international capital movements. The fortunes of the U.K. reserves during the war are likewise divisible into <sup>in this case</sup> (three) broad periods - not influenced by capital movements in the same sense, but by an external Balance of Payments (current transactions) of unprecedented dimensions, and increasingly adverse to the U.K.

First, there was the need to meet, unaided, the payment for very large supplies from overseas to supplement greatly intensified, but still far from adequate, home production during the first  $1\frac{1}{2}$  years of war. In this, the 'bash and carry', period the drain was inevitably so largely in dollars that by March 1941, on the eve of Lend-Lease, our gold and dollar holdings had become insignificant.

The second period, beginning with all-but-exhausted reserves at the point where Lend-Lease began to operate, may be said to have ended about  $1\frac{1}{2}$  years later (in the late Autumn of 1942), by which time the U.K. Authorities were taking counsel among themselves as to the best means of preventing reserves, already approaching £200 million, from exceeding £250 million within the next six months. The main contributory factors to this increase were -

- (a) The continued sale of gold by South Africa, partly offset by certain sales elsewhere.
- (b) The virtual cessation, under Lend-Lease, of cash payments to the U.S.A.
- (c) The expenditure of U.S. troops, now filtering in large numbers into almost every part of the Sterling Area (expenditure in 1942, say, \$250 million).

The first

The first two periods are in well-marked contrast.

The third has really three phases, though they are not so clearly definable. From early 1942 a rapid replenishment of reserves as a result of Lend-Lease was an embarrassment because Lend-Lease itself might be jeopardised as the increase (particularly in dollars) became known and criticised in America; and the authorities therefore sought suitable liabilities (e.g. certain kinds of Blocked Sterling) to pay off, and began to widen the scope of Registered Sterling. On the other hand consciousness of rapidly growing sterling liabilities dictated the need to accumulate proportionate reserves to meet them - a case which was only made convincing to the Americans after continued and patient representation. Two conflicting motives thus existed side by side for a time; but the means to prevent a too rapid increase in dollars had been decided upon by the Autumn of 1942, while the other principle was being contested well into 1944.

The third phase may be said to begin where the latter principle became accepted, and to pass later and almost imperceptibly into the end of Lend-Lease and the U.S. Loan negotiations, and later still into post-war conditions - a rapidly deteriorating balance of payments culminating in the convertibility crisis of the Summer of 1947.

As the war (and the all-important financial arrangements between the U.K. and the U.S.A.) progressed, the accepted concept of "reserves" came to be exclusively U.S. dollars and gold, at first "gross" and later "net",\* and the following details are confined to gold and U.S. dollars (gross).

Period (1), extending from 3rd September 1939 to 31st March 1941, accounted for a net worsening of the reserve position by £426 million and left reserves of only £66 million (on 31st March 1941). Period (2), beginning from 1st April 1941, saw a net increase of £169 million to £235 million on 30th September 1942. The essentials in the changed position over these periods were:

Spot Holdings

---

*after deduction of later liabilities*  
 \* i.e. ~~including U.S.A.~~ and Registered Sterling liabilities: for further explanation see under "Financial Relations with U.S.A."

S  
Spot Holdings (gold at 168/- per oz.fine)

(1)

3rd September 1939 - 31st March 1941

£ million

Held on 3rd Sept. 1939:

Gold		479
U.S.\$		<u>13</u>
		492

Transactions 3rd Sept. 1939 - 31st March 1941:

Gold bought		229
" sold (for U.S.\$	552	
(other disposals	<u>125</u>	<u>677</u>
		-448
		44
U.S.\$: net purchases		<u>22</u>

Remaining (spot) reserves on 31st March 1941

		66
of which (Gold (excluding 25 borrowed from Belgium)		<u>31</u>
(U.S.\$		35

(2)

1st April 1941 - 30th September 1942

Held on 31st March 1941:

Gold		31
U.S.\$		<u>35</u>
		66

Transactions 1st April 1941 - 30th Sept. 1942

Gold bought		199
" sold (for U.S.\$	37	
(other disposals	<u>26</u>	<u>63</u>
		136
		202
U.S.\$: net purchases		<u>33</u>

Remaining (spot) reserves on 30th Sept. 1942

		235
of which (Gold (excluding 25 Belgian)		<u>167</u>
(U.S.\$		68

The third period may be regarded as ending (some months after the defeat of Japan but at a convenient date statistically) on 31st December 1945; and the full third period as extending for  $3\frac{1}{4}$  years from 1st October 1942 until that date. Following the same detail as was shown for the two earlier periods, the figures are as follows (gold at 168/-):-

(3) 1st October

(3)

1st October 1942 - 31st December 1945£ millionHeld on 30th Sept. 1942

Gold (spot - excluding 25 Belgian)	167
U.S.\$	<u>68</u>
	235

Transactions: 1st Oct. 1942 - 31st Dec. 1945

Gold bought	512*	
" sold (for U.S.\$	(Nil.)	
{ other disposals	<u>201</u>	311
U.S.\$: net purchases		<u>48</u>

Remaining reserves on 31st Dec. 1945 594

of which (Gold	477
(U.S.\$	117

Of the first two periods there seems little need to say much here: they are sufficiently contrasted and the figures tell their own story. The third period perhaps requires rather more comment, though the stages in our long discussions with the U.S.A. and the resulting arrangements are fully dealt with in "Financial Relations with the U.S.A.", which should be read in context with this chapter.

The rapid growth in reserves in 1942/43 resulted almost entirely from Lend-Lease and from U.S. Forces' disbursements in the Sterling Area.\*\* Liabilities increased mainly because of the spread of the war eastwards, though commitments to European "neutrals" (pre-emption of essential materials) and to South and Central America (foods and raw materials) were very heavy. The eastward movement of H.M. Forces inevitably gave very large sterling claims to Egypt, India, etc., so that the greater part of the growth in liabilities was to the Sterling Area. From early 1943 onwards the U.K.

authorities

\* of which 158 for U.S.\$

\*\* In the 18 months Jan. 1942 - June 1943, of a total net increase in dollars of \$635 million, dollars received from the rest of the Sterling Area accounted for \$594 million, of which the greater part represented U.S. troops expenditure. Nearly another \$100 million arose from receipts in the U.K. from U.S. Forces. (H.M.T. memorandum 14.9.1943, for presentation to the U.S. Government.)

authorities devoted much thought, made numerous journeys and undertook many difficult negotiations in order to convince the Americans that we had to face a formidable problem in the ultimate liquidation of these liabilities; and that our position as the traditional bankers to Sterling Area creditors provided no comprehensive solution.

As mentioned above, certain measures designed to act as a brake on the rate of growth in dollar and gold holdings began to operate before the end of 1942; others, not until the following year. In November 1942 a first release of blocked sterling (£12½ million on account of film royalties etc.) was made; and the principle was extended shortly afterwards to certain claims of a capital nature.\*\* In June 1943 sales of gold in the Middle East and India began (they ceased in January 1945). Meanwhile there was no abatement of the long argument in support of the principle of maintaining adequate reserves.

A table of Reserves, including also Canadian dollars and Other Currencies, is appended, shewing the spot position immediately before the outbreak of war (2nd Sept. 1939) and at the end of each quarter from December 1939 to December 1945. After December 1939, when £17.6 million in Canadian dollars were held, this figure ranged between £2 million (Sept. 1941) and £10.1 million (Sept. 1945); Other Currencies between £1.6 million (all French francs) at the outbreak of war and £30.8 million in March 1945, of which £16.2 million in French francs. Total reserves were highest in March 1945 at just under £660 million.

---

\*\*See under "Blocked Sterling".

Reconciliation of Changes in Reserves with the Balance of Payments

Under the Gold Standard a balance of external payments adverse to the U.K. would have been adjusted by an outflow of gold, and a favourable balance by an inflow: in the war (and indeed since September 1931) an increasingly adverse balance drew predominantly on <sup>official</sup> Reserves, while the period of Lend-Lease enabled additions to them to be made. The operation of the Gold Standard, it is true, was automatic and incidentally exercised an internal control over the currency, absent since its suspension and replaced by other <sup>measures</sup> ~~measures~~. But there remained, at least until the coming of Lend-Lease and Mutual Aid, a similar close relationship between an excess of overseas expenditure over receipts and the draft on reserves required to meet it.

Deficiencies in the statistical detail of payments and receipts are alone responsible for the lack of a complete picture of the processes by which the account is settled - deficiencies which are inherent in the nature of many of the transactions themselves and the difficulty or impossibility of collecting the necessary data, but which arise also because the dates and periods for which data are available do not correspond. It is sufficient to mention the lag between dates of recording and of paying for shipments of goods; though its effect, it is true, can be lessened by the adoption of certain conventions. Other measurements are altogether elusive - many kinds of capital movement, for example. Nevertheless, a good deal can be done towards reconciling the (known) changes in Reserves and the (incompletely known) Balance of Payments items for a given period.

From an early date in the war\* as close a record as possible of all known Balance of Payments elements was kept, and eventually became the basis of a more or less standardised framework, continually improved and extended geographically, for the progressive study of the Balance of Payments.

A comprehensive

---

\*The Statistics Section of the Exchange Control was set up in September 1939, and the Exchange Economy Section (later incorporated in the Overseas and Foreign Office) in March 1940. Both were absorbed by the Statistics Office in March 1942. (See also under "Control in Practice").

A comprehensive account, at least, of Sterling Area payments in hard currencies was a strong foundation on which to build; and this had become available through the development of an analysis of the results of classifying currency and sterling application forms (E and E1.), geographically and according to purpose.

Eventually (in 1942) a regular report, with figures at quarterly intervals and forecasts for two or three quarters ahead, came into being. It was discussed at D.(F.) R. Committees at the Bank and then passed on to certain officials of H.M.T. for their entirely confidential use. Later, parts of this document, familiarly known as the "dossier" - its full title was "Report on Exchange Position and Balance of Payments Estimates" - were made available slightly more widely, e.g., to the Chief Statistician of the Board of Trade.

It is unfortunately not possible to link these quarterly figures closely enough with the more accurate detail on Reserves for a satisfactory comparison to be made in periods (1) and (2) above; but an attempt is made below to reconcile them over a series of years, including the war. The table covers the last four months of 1939 and calendar years thereafter; it endeavours to carry back as far as possible the scheme (condensed for simpler presentation) of the latest White Papers on the subject. (Division of liabilities into Sterling Area and non-Sterling Area is not possible before 1942.)

The figures illustrate only too clearly the extent to which an accumulated deficit of over £5,700 million has been financed by incurring external indebtedness, including in 1946/47 the U.S. and Canadian credits. *It may be convenient first to give a summarised version shewing the war years and the years 1946 and 1947 as two separate periods.*

<u>£ million</u>	<u>U.K. Balance of Payments.</u>	
	<u>1939-45</u>	<u>1946-47</u>
Deficit	4,744	1,000
met by:		
Decrease in Reserves	187	100
Realisation of External Capital		
<u>Assets.</u>	1,120	(increase) - 6
Increase in External Liabilities	3,251	966
Miscellaneous items	186	(increase) - 60
		<u>U.K. BALANCE</u>

U.K. BALANCE OF PAYMENTS

U.K. BALANCE OF PAYMENTS

£ millions

FINANCED BY: -

U.K. Deficit on Current Account		Decrease or Increase (-) in Reserves(a)	Increase in External Liabilities		Realisation of External Capital Assets		Miscellaneous (d)	
			Decrease (-)	Decrease (-)		Sterling Area		Non-Sterling Area
				Inside Sterling Area	To Non-Sterling Area			
Sept.-Dec.	1939	212	57		80	7	50	18
Year	1940	811	474		179	42	109	7
"	1941	820	- 23		564	113	145	21
"	1942	674	- 75	351	168	130	97	3
"	1943	689	- 150	468	179	136	51	5
"	1944	663	- 99	513	95	43	83	28
"	1945	875	3	527	127	59	55	104
"	1946	370	- 52	- 37	372 <sup>(b)</sup>	25	46	16
"	1947	630	152	- 166	797 <sup>(c)</sup>	- 64	- 13	-76 <sup>(e)</sup>

(a) Changes in reserves for 1939-45 are as published in Cmd.6707 of 1945 and Cmd.7099 of 1947 and relate to gold and U.S.dollars; figures for 1946 and 1947 are as published in Cmd.7520 of 1948 and relate to gold, U.S. and Canadian dollars.

(b) Includes U.S. and Canadian Credits 279.

(c) Includes U.S. and Canadian Credits 812.

(d) Includes unidentified inflow or outflow of Capital to or from U.K. (very large outflow in 1947); changes in purchases of U.K. Securities by foreigners and in odd working balances in U.S.dollars and in all other currencies held on E.E.A/c; adjustment for cost and proceeds of gold at actual price of transaction (as opposed to valuation under Reserves); sundry other adjustments (small)

(e) Australian and New Zealand gifts (+ 30) and drawings on I.M.F. (+ 60) are subsumed in this figure.

406

## E.E.A. HOLDINGS: SPOT

£000's

	Gold @ 168/- per fine oz.	U.S.\$ @ 4.03	Can.\$ @ 4.45	All other Currencies
At 30th June 1932	22,460	2,797	-	-
30th Sept. "	41,556	11,533	-	1,537
31st Dec. "	43,108	24,870	-	3,213
31st March 1933	95,413	32,552	-	295
30th June "	117,861	27,588	-	893
30th Sept. "	52,168	14,451	-	875
31st Dec. "	116,945	776	-	605
31st March 1934	144,479	508	-	205
30th June "	142,414	250	-	302
30th Sept. "	107,096	417	-	283
31st Dec. "	114,172	517	-	263
31st March 1935	118,289	476	-	243
30th June "	165,267	479	-	228
30th Sept. "	207,352	510	-	258
31st Dec. "	191,620	1,180	-	501
31st March 1936	236,608	1,047	-	214
30th June "	314,873	1,051	-	156
30th Sept. "	294,047	226	-	95
31st Dec. "	213,657	6,334	-	311
31st March 1937	223,898	293	16	321
30th June "	300,371	1,839	10	272
30th Sept. "	334,778	3,072	10	363
31st Dec. "	348,200	4,440	441	246
31st March 1938	357,385	3,060	128	870
30th June "	303,232	4,821	301	718
30th Sept. "	191,185	5,961	65	722
31st Dec. "	44,854	7,668	214	1,574
31st March 1939	424,343	17,769	860	508
30th June "	357,247	25,474	482	1,211
30th Sept. "	463,483	53,269	1,949	2,106

Capital

(000's omitted)

25th June 1932	From old Exchange A/c (as finally adjusted)	£24,999
	From Consolidated Fund	<u>150,000</u>
		£174,999
20th May 1933	From Consolidated Fund	<u>200,000</u>
		£374,999
7th July 1937	From Consolidated Fund	<u>200,000</u>
		£574,999

Cashier's Department (Exchange Control & Overseas),  
Dealing & Accounts Office,  
Books & Statements Post,  
27th May 1949.

SECRET

## E.E.A. HOLDINGS: SPOT

£000's

	Gold @ 168/- per fine oz.	U.S.\$ @ 4.03	Can.\$ @ 4.45	All other Currencies
At 2 Sept. 1939	479,039*	13,109	1,706	1,613
" 31 Dec. "	490,690	36,829	17,628	2,764
" 31 Mar. 1940	467,247	19,748	4,102	2,580
" 30 June "	363,293	24,351	2,136	12,021
" 30 Sept. "	193,735	25,946	3,656	12,747
" 31 Dec. "	70,495	32,611	5,119	12,320
" 31 Mar. 1941	30,793(a)	35,453	3,294	12,642
" 30 June "	20,679	40,680	3,669	12,015
" 30 Sept. "	43,357	24,109	1,994	11,980
" 31 Dec. "	100,480	37,239	3,285	12,536
" 31 Mar. 1942	132,469	28,617	2,003	13,951
" 30 June "	153,906	46,238	4,871	14,660
" 30 Sept. "	166,588	68,564	2,797	13,049
" 31 Dec. "	167,134	81,914	4,667	13,027
" 31 Mar. 1943	219,553	72,247	4,020	12,977
" 30 June "	235,874	112,920	3,633	12,792
" 30 Sept. "	235,991	162,006	3,152	22,250
" 31 Dec. "	252,354	199,447	4,735	21,040
" 31 Mar. 1944	285,617	213,317	5,055	23,204
" 30 June "	339,823	226,370	5,128	16,906
" 30 Sept. "	396,935	185,552	6,688	19,721
" 31 Dec. "	422,396	173,836	5,189	21,761
" 31 Mar. 1945	431,537	165,530	5,543	30,835
" 30 June "	441,723	168,016	3,066	25,967
" 30 Sept. "	447,240	134,245	10,074	25,533
" 31 Dec. "	476,965	116,941	4,418	7,481
" 31 Mar. 1946	486,616	83,927	4,574	18,238
" 30 June "	513,095	31,821	8,698	26,705
" 30 Sept. "	554,478	80,475	7,698	36,706
" 31 Dec. "	582,889	54,866	6,397	40,669
" 31 Mar. 1947	543,252	25,680	3,478	39,657
" 30 June "	567,381	9,716	1,896	39,782
" 30 Sept. "	546,670	20,918	4,626	38,504
" 31 Dec. "	481,809	11,315	5,930	36,847

\*Including 278,965 held by Issue Department.

(a) Gold holdings from 31st March 1941 to 31st December 1942 inclusive exclude £25.2 millions borrowed from Belgium.

£ MILLIONS

# RESERVES

E.E.A. HOLDINGS

