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GERMANY AFTER THE SECOND WORLD WAR AND ITS PLACE IN THE COMMON MARKET.

Introduction.

Historians have always found German history more difficult to write than any other, because they contend that Germany possesses no inner unity either as a State or as a nation. What has customarily been described as "Germany" is a generec term more of a geographical than of a political nature. The German nation-State created by Bismarck in 1870 - 1871 was styled the "German Reich", a title imitated from the old "Holy Roman Empire of the German Nation", although the two polities were demographically, territorially and constitutionally wholly dissimilar. The name was retained up to 1945.

In referring to "Germany" today we have to make it clear exactly what we intend by the expression. To cover the whole of Germany we have to include five separate territories. First, there is the Federal Republic of Germany, which enjoys almost complete national autonomy and a constitution which came into force in 1949, providing for a Federal President as head of the State, a Federal Chancellor as head of the Government, a Federal Parliament and a Federal Council representing the constituent Länder. The Federal Republic is a confederation of ten Länder, each with political, economic and cultural powers but no independent foreign, monetary or military sovereignty. It covers an area of 248,000 square kilometres with a population of 51 million, and extends eastward from France, Belgium and the Netherlands to the River Elbe, and southward from the North Sea to the Alps.

East of the Elbe as far as the Polish and Czechoslovak frontiers lies an area of 107,000 square kilometres, with a population of some 17 million, which goes by the name of the German Democratic Republic. This State was brought into being by the occupying Power, the Soviet Union, in 1949, on the basis of a constitution imposed by that Power. Its sovereignty is recognized only by the countries of the Eastern bloc and by Jugoslavia, not by the Western Powers or the Federal Republic. It is divided into fourteen administrative districts.

The legal position of Berlin is obscure. It had a special status even under the Empire and the post-1918 Weimar Republic. After the second world war it became a unit made up of four separate sectors, and in November 1948 it was divided by the Russian-controlled Communist Party into two parts.

Also without a properly-defined legal status is the area east of the Rivers Oder and Neisse, which is under Polish administration. So too is that part of the former province of East Prussia which was annexed by Russia in 1945, again without benefit of treaty. For so long as no peace treaty has been concluded between the former belligerent powers, the Federal Republic, reasonably enough, regards the provisional administrative regime in these territories as an illegal annexation.

Finally, there is the Saar, which by the terms of an agreement between the Federal Republic and France became part of the Federal Republic on January 1, 1957, but is to be economically integrated into it only in the course of the ensuing three years.

The Beginnings

The war unleashed by Hitler in 1939 ended in May 1945 with the full achievement of what the Allies had proclaimed as their main war aim - the unconditional surrender of Germany. After Hitler's suicide there was no national authority, no Government, not even a unified economic system. Instead there was a military occupation administration, or rather four military occupation administrations, with the monster job of acting as the German Reich's receivers in bankruptcy. Before they had completed it, the general historical truth had been abundantly borne out that it is easier to win a war in the field than to conclude a successful peace. At the Potsdam summit conference - as we should call it noadays - in 1945, Harry Truman, Winston Churchill and Clement Attlee, and Joseph Stalin agreed that Germany should remain an economic unit. All four zones of occupation were to contribute their share to overall German production and derive their share from it. A plan for industry drawn up by the Allies in March 1946 provided that all plant over and above a specified total capacity was to be dismantled, and that there was to be a regular interzonal exchange of production. This plan, which was largely influenced by the completely unrealistic Morgenthau Plan, was based on the principle of restricting German economic potential to a bare subsistence level. It is one of the ironies of history that the Americans were the first to realize its impracticability, and promptly decided to turn right-about. But we must not neglect to pay tribute to the vision and courage in particular of the two American High Commissioners, General Clay and Mr. McCloy, whose work was of the greatest importance to the reconstruction of Western Germany.

The plan had not been long adopted before it became apparent that the Russian occupation authorities were not prepared to fulfil their obligations under it. The practically hermetic sealing of the border between the Russian and the three Western zones, the suspension of westbound deliveries, the blockade of Berlin in the autumn of 1948, all impelled the three Western Allies to make repeated changes in the dismantlement plan so far as their own zones were concerned, and to raise the scheduled industrial capacity. Further Russian endeavours to seize power in the Western democracies decided the United States, with the agreement of Britain and France, to allow Western Germany to benefit under the Marshall Plan. June 1948 saw the American-sponsored reform of the German currency. General political and economic developments finally gave the Western Allies ample reason to combine their three zones of occupation into a single economic area.

The rest of my remarks will be concerned with the economic development of the Federal Republik since 1948-1949.

Population, Employment and Production

The capitulation in 1945 and the territorial and demographic measures which followed hit the German economy very hard indeed. The Potsdam decisions lopped off something like one-quarter of the German Reich and 14% of its population. The great majority of the inhabitants were expelled from the areas concerned and had for the most part to come to the Western zones in search of a livelihood and a roof over their heads. The position in 1946 was as follows:

Territory	sq.km.
Area of the Reich as in 1939 (exclusive of Austria and the Sudetenland)	approx. 482,000
Four zones plus Berlin of which:	357,061
Soviet Zone	107,481
Berlin	884
Western Germany	248,696

Population	'000 1939	'000 1946
Area of the Reich as in 1939	69,460	--
Four zones plus Berlin of which:	59,794	65,930
Soviet Zone	15,160	17,333
Berlin	4,339	3,180
Western Germany	40,295	45,417

The loss of the agricultural-surplus areas in the East and the simultaneous expulsion of the inhabitants was regarded in the early days as a completely crippling burden on the economy. Industrial production in what was to become the Federal Republic amounted in 1946 to only one-third of what it had been in 1936. Exports in that grim year totalled no more than about $ 200 million; imports came to nearly $ 700 million and something like two-thirds of them were paid for with the help of the Western occupying Powers. Germany seemed doomed to remain for years to come the pensioner of her former adversaries.

In retrospect, it is obvious that the revival since the currency reform could probably never have been achieved had it not been for the influx of refugees and expellees. The resultant manpower surplus was one of the sources of what has since been called the German economic miracle. Its economic importance really lies in the fact that only thanks to it was an expansion in the production of goods and services possible in the first place. Then the increase in population and the gradual reintegration of the people concerned into the labour cycle laid the foundation for a rise in the income of the masses, and thereby for a steady expansion in demand. The considerable leeway to be made up, coupled initially with a certain lack of inclination to save, and the consequent impetus to production resulted in a cumulative expansion of the home market. There came into play what economists today term the multiplier effect and the accelerator effect. In addition, the size of the manpower reserve acted as a check on wage claims, the wage level and labour costs. One of the major prerequisites for the strengthening of the Federal Republic's competitive capacity in the world market was thereby secured.

And now a few facts and figures.

From 1949 to 1956 the Federal Republic received more than ten million refugees and expellees. The total population of the area, inclusive of the Saar, which in 1939 had been about 40 million, had risen by 1956 to 51 million; the actove population (exclusive of unemployed but inclusive of military personnel) rose from rather over 20 million in 1950 to 24.6 million in 1957. The real yearly rate of increase in the gross national product over the period 1950-57 was 7.9%, and the rate of those actually in gainful employment 2.9%. Output per active-employed person -- commonly referred to, not altogether accurately, as labour productivity -- thus increased by approximately 5 % per annum. In the remainder of my talk I shall use the expression "productivity" for the sake of terminological simplicity, but I must ask you to bear in mind that it would be equally instructive to consider the increase in overall production in relation to capital.

One is tempted to attribute the increase in productivity first and foremost to the passionate will to work, the innate discipline and the organizing ability of the Germans. It is common knowledge that work is almost a religious vocation in Germany: moreover, the German people during the immediate post-war period undoubtedly did work very hard indeed -- presumably even harder than the figures indicate. And yet statistical analysis brings out the complexity of the relations between production, employment and output.

If we take the currency reform as marking the beginning of the expansion, industrial production at that time, in mid-1948, was only half what it had been in 1936, a year of medium activity. The level was appreciably lower than it need have been given the industrial capacity available. Western Germany, which before the war had had 56 % of the total population of the Reich, found itself as a result of the division into East and West with about 61 % of the former industrial capacity. War damage to production plant and machinery was certainly very considerable, and up to then only very little of it had been made good; yet it was possible for a not too considerable outlay, and in some cases quite a small one, to make the necessary repairs and increase production rapidly. And it is a fact that within the first six months of 1950 industrial production reached its 1936 level, and continued rising thereafter until in 1957 it was two and a half times as high.

At the beginning of this period of expansion the number of unemployed was very high: in 1950, for instance, the proportion was as much as 10 % of the active employed persons. Between 1950 and 1957 the number of employed increased as a result of immigration, school-leavings and the use of female labour by 4.6 million, or nearly one-quarter; the number of unemployed fell by 900,000, and by 1957 amounted to only 3.4 %. A breakdown of the growth of overall economic production, that is, of the gross national product, shows that at the beginning of the period the share of productivity was very high. Up to 1955 it rose year by year from 4 to 8 %, while the annual rate of increase in the number of employed was 2 to 3 %. Since then, however, the two trends have tended rather to converge, so that in 1957 the contribution to the gross national product deriving from labour-force intake and from increase in productivity was nearly equal.

The labour productivity of the economy as a whole can be increased either by workers transferring from the low-efficiency sectors to the high-efficiency and consequently highly-paid ones, or by immigrant workers entering predominantly the high-efficiency sectors. In the Federal Republic both these things have been happening. The number of persons employed in agriculture and forestry fell between 1950 and 1957 by close on a million, or nearly one-fifth; the number of persons employed in industry rose by more than three million, or over one-third, and the number in the tertiary sector also increased substantially. Early on there was a tremendous increase in agricultural productivity, but this has remained more or less stationary since 1955: the converse occured in the industrial and particularly in the tertiary sector.

May I recapitulate briefly: Once the restrictive provisions of the 1946 plan for industry had been rescinded, willingly or unwillingly, by the occupation authorities, and the division of Germany had proved less disastrous for the economies of the Western zones than had at first been feared, it was possible, with the abundant manpower reserves available, to get such production plant as remained into working order again fairly quickly and thereafter progressively to expand it. In the early period in particular the Germans' passion for work was very much in evidence and stood them in good stead. Later, other developments supervened, some of them outside Germany's borders, which served to consolidate the work of reconstruction. The most important point in this connection is to arrive at an assessment of the role of German economic policy.

Orientation of economic policy

It was not until the currency reform of June 1948 that there was an economic policy worthy of the name in post-war Germany at all. What was then introduced was in its outlines the work of American experts, but it created, and thereafter continuously extended the scope play for the West German economic administration and, from September 1949 onwards, for the Federal Government.

The object of the currency reform was to eliminate the then grave disproportion between the money and the goods in circulation by drastically reducing the supply of money. To do so, it was not enough simply to fix a new par of exchange: public and private liabilities had to be entirely reorganized. There was an overall reduction in the value of the mark from 100 to 6.5. The currency reform led on to a tax reform and to the progressive abolition of price-controls and rationing; later came assistance to refugees and expellees and compensation of victims of National-Socialist persecution.

The economic policy of the Federal Republic has been greatly influenced by a neo-liberal economic science which has come to be known as "Soziale Marktwirtschaft". It would go beyond the purpose of my talk today if I were to try to explain this system in detail, particularly as it embodies not only economic principles proper but also concepts of social philosophy relating to order (in the Latin sense of ordo). It is essentially based on the ordering of society through competition, and thus through free pricing and free access to production and means of production. Such an order demands stable currency, freedom of competition -- that is, no cartels or monopolies -- and freedom in the development of foreign trade. A competitive economy unhampered by monopolies, cartels and distorting State intervention may reasonably be expected to ensure the most advantageous, and therefore socially equitable, distribution of income. Distribution of income is determined by the marginal productivity of the production factors, and is hence socially satisfactory to the extent that each individual receives the equivalent of what he has himself contributed to the national product.

Soziale Marktwirtschaft is very much in contrast to another school of modern economics, which advocates not "orders" but economic models aiming at the vigorous development of production by centralized planning of investment and foreign trade, at full employment and at an equitable distribution of income. It would be extraordinarily instructive to trace the reasons which impelled the Federal Republic to choose the first doctrine rather than the second. It is doubtful whether the inclination and decision were all along as well defined as their subsequent vindication would suggest. The first Federal elections in August 1949 can hardly be interpreted as a straight pronouncement by the electorate for or against Soziale Marktwirtschaft, although certain of that system's fundamental principles, such as currency stability and the abolition of controls, were generally approved. But the speed with which reconstruction proressed in the years that followed is in many respects proof positive of its validity: at later elections up to 1957 they voted overwhelmingly for its representatives the Cristian Democrats, and more and more against the Socialist Party.

Almost a stroke of genius, undertaken against Allied advice, was the early and systematic ending of rationing. Another determining element was the insistence on a stable currency, which was achieved in the teeth of a good many inauspicious circumstances. Also of great importance was the priority given to the expansion of production capacity -- that is, to investment. And of course we must not forget that the ever-widening gulf between East and West has also played its part in bringing the economic recovery of the Federal Republic so conspiciously before the public eye.

Investment, Consumption and Income.

Outstanding among the factors responsible for the swift expansion of the Federal economy is the high rate of investment and savings. While gross national income (at constant prices) increased between 1950 and 1956 by 63 %, capital expenditure on fixed assets alone, i.e. without inventory, increased by 84 %. The overall quota of gross investment inclusive of inventory amounted during these years to 22 to 24 % of gross national product.

This is of further significance inasmuch as there has never been such a thing as a general German investment programme: in fact, those with whom the matter rested were explicitly opposed to any planning of investment whatsoever. At most one-fifth of gross capital expenditure came from public funds, and only one-half of that was centrally administred. Housing and public works were the two sectors which were to some extent State-aided and State-directed, and even there aspects other than the encouragement of all-round expansion, or even the offsetting of market fluctuations were on the whole given prior consideration. It is therefore of interest to try to examine how the upward trend in investment was induced in the first place, and how it was then handled financially and encouraged.

The fact that there was no centralized planning and no financing of investment by means of State credits did not necessarily mean that there was no orientation of investment at all. One extremely effective form of guidance was provided by fiscal policy. At the beginning of the reconstruction period the burden of taxation was exceedingly heavy and made more so by the steep progression of tax rates on higher incomes. The fiscal authorities, however, introduced generous tax allowances and reliefs favouring in some cases general capital formation and in others the channelling of capital into particular sectors, such as the building trade and the shipyards.

This method of financing investment has been widely criticized. Objections have been heard that it is leading to misorientation of the flow of capital: for instance, it has been held responsible for the emergence of bottlenecks in the coalmining industry and in the public utilities. These objections should, however, be raised more against price policy than against fiscal policy. Although the Federal Government took controls off most prices, those of coal, electricity and gas, and for a long time of steel, continued to be officially controlled and fixed for a long time. Tax reliefs in these sectors remained inoperative, as returns were not developing as they otherwise would have done.

It is not too easy to rebut the further charge that this taxation system puts a premium on self-financing of investment by way of prices, and thereby on maldistribution of property. Criticism has been levelled from within the German economy itself at the unjustifiably high tax rates, the accumulation of the proceeds in public funds and the consequent redistribution of burdens.

A comparison of net savings and net investment may help us to form a better judgment of the pros and cons.

	1950	1952	1954	1956	1957
	in % of net national product at market prices				
National net investment					
Capital assets	13,9	13,0	14,5	16,0	13,7
Inventory stocks	1,2	4,2	3,7	3,2	2,2
Foreign investment	-0,1	2,1	2,0	1,9	2,9
	15,0	19,3	20,2	21,1	18,8
National net savings					
Private sector	2,6	3,9	5,1	4,2	5,8
Commercial and industrial sector	6,6	9,3	7,0	7,8	5,5
Public sector	4,0	5,9	8,0	9,4	7,8
	13,2	19,1	20,1	21,4	19,1
Capital transfers from abroad	1,8	0,2	0,1	-0,3	-0,3

In no year between 1950 and 1956 did the private sector contribute more than one-quarter to total net investment. To begin with it was largely industry which financed investment; from 1953 on the State also came very much to the fore. Of a net 35 billion marks invested in 1956, 45 %, or 16 billion, came from the savings of public authorities. Only about one-third of these savings went on actual public investment: the other two-thirds were represented by balances at credit institutes, securities and so on, so that the moneys extracted from the economy by high taxes flowed back to it via the banking system and capital markets. Self-financing by enterprises, which from 1950 to 1952 had accounted for over 60 % of net investment, later dropped to 46 to 47 %. Absolutely speaking, this is very high. Admittedly, it is not to be attributed only to the peculiarities of the fiscal system: the fact that the enterprises have comparatively little capital of their own probably has a good deal to do with it.

This last point is borne out by a further calculation. If we take the marginal capital output ratio - that is, the movement of gross, or alternatively of net investment in relation to the movement of gross, or as the case may be net national product - we find that in the Federal Republic it is only half as great as in the other Western European countries, which indicates that the allround economic expansion has been possible mostly thanks to the employment of a comparatively large labour force. It is further apparent, however, that private saving has been very much influenced by the structure of the fiscal system. I refer more particularly to the considerable accumulation of savings by the social insurance institutions, and also to those forms of savings which enjoy certain tax allowances, such as life insurance, saving banks for housebuilding, etc.

And finally, we find that the large accumulation of public savings in 1955-1956 in particular took the form of an increase not in the flow of capital to private enterprise at home, but in an increased ratio of net foreign investment (inclusive of increase in gold and currency reserves).

By and large, the period from 1950 to 1955-56 was a time of recuperation, starting low indeed and even by the end not quite level with the other countries of Western Europe. Towards the end of my talk I shall deal with the extent to which Western Germany's position has since changed and the implications of this for the future expansion of its economy.

The very marked concentration on investment and, in particular, on exports, is accompanied by a comparatively modest rate of consumption. From 1950 to 1956 gross national product (at constant prices) increased by 63 %, private consumption by approximately the same, and Government consumption by only 29 %. If we reckon these percentages in terms of current prices, the share of both private and public consumption in the gross national product actually fell.

Post-war German economic policy has often been represented as uncommonly tough. All sorts of arguments have been adduced in support of this view. Even the West German trade unions have repeatedly complained that the workers have not been given their rightful share in the country's economic recovery, although it is undoubtedly true at the same time that they have shown considerable restraint in their wage claims and thereby greatly assisted the process of reconstruction.

A comparison of the trend in national income with that in private income from salaries and wages, on the one hand, and from property, on the other hand, works out as follows:

	National income	Private income from salaries, wages, etc.	Private income from business activity and properties
	1950 = 100		
1951	122	121	127
1952	136	135	125
1953	146	149	127
1954	157	163	139
1955	180	186	157
1956	197	208	165

In general the Unions have not done badly in spite of their restraint, for, as the figures show, incomes from salaries and wages have risen more steeply than national income. This is, admittedly, due in the main to the increase in the number of employed. The average net income per worker employed increased between 1950 and 1956 by only 55 %. There are a number of reasons which explain this statistically - the increase in the proportion of female labour (in the Federal Republic women are paid less than men), the employment of elderly and partially unfit workers. All things considered this only bears out the principle I mentioned earlier, that in post-war Germany everyone simply received the equivalent of what he had himself contributed to the national product. Viewed from this angle, German economic policy was indeed tough. But we have to remember that it had to carry a big group of annuitants, old-age pensioners, etc. Real social distress was alleviated as far as possible, and however inadequate the relief actually afforded to individuals, the social budget accounted after all for something like 40 % of the public budget.

Foreign Trade an Payments and Foreign-Trade Policy.

Non-Germans are more struck by the restoration of the country's foreign trade position than by the resurgence of its internal economy. The reference to the "German economic miracle" is principally based on the fact that the D-mark has for years been a hard currency - harder than sterling - and that the Federal Republic today ranks third, or even second, among the great exporting countries of the world. And if we bear in mind that German foreign trade had to start absolutely from zero after the collapse and was until the currency reform administred by the occupying Powers, and furthermore that up to 1950 a considerable proportion of German imports had to be paid for by foreign aid (mainly from the United States), well, indeed it does seem almost like a miracle.

From 1949-1950 onwards reconstruction went ahead, not of course without some inital setbacks, but on the whole steadily and swiftly. Exports more than quadrupled betwen 1950 and 1957, imports almost trebled. The amounts received and/or paid in services increased tenfold. The combined trade and services balance in 1950 showed a deficit of more than one billion dollars, and in 1957 a surplus of something like eighteen hundred million dollars. As regards gratuitous deliveries and remittances - represented mainly by foreign aid to the Federal Republic and restitution payments by it - at the beginning of the period nearly one billion dollars more came in than went out, and in 1957 nearly 400 million dollars more went out than came in. Finally, as regards capital movements, other countries in 1950 provided a total of 100 million dollars, whereas in 1957 the Federal Republic lent one billion dollars more to other countries than they did to it. All in all, there was a currency debit balance of approximately 150 million dollars in 1950 and a credit balance of 2,200 million in 1957, and the Central Bank's gold and currency reserves had risen from their inital figure of 150 to 200 million dollars to something like 5,500 million dollars at the beginning of 1958.

During these seven or eight years, world trade turnovers increased by about 70 %, while the Federal Republic's volume of foreign trade (imports plus exports) multiplied by three and a half. Part of this increase may therefore be explained comparatively straightforwardly as arising out of the upsurge in world trade: German foreign trade was caught up in a world-wide process of expansion. At the beginning of the period the German share in world exports was only about 7.5 %, or approximately half what it had been in 1937. The Federal Republic thus had to start from a very low level indeed, and it was not until 1955 that it regained its pre-war percentage.

At the beginning of the period with which I am concerned, there was a serious shortage of capital goods throughout the world. Germany has always been an exporter of capital goods. The Federal Republic was particularly well placed to help meet the demand elsewhere inasmuch as it had retained a comparatively large proportion of the capital-goods industries after the division into East and West. And, even after the division there was a steady transfer of scientific and technical experience, skilled personnel and even essential items of industrial equipment from the Eastern Zone to the Federal Republic. And last but not least Germany did not have any expenses in connection with armaments. So one way and another there were quite a number of circumstances favourable to the building-up of the export trade.

On the other hand, Germany has not surpassed its pre-war share in world trade to any appreciable degree. We may see this fairly clearly from, for instance, a comparison of exports of finished products by the main exporter countries.

Exports of Finished Products by Main Exporter Countries[1]
(in % of total)

Country or group of countries	1937	1951	1952	1953	1954	1955	1956[2]
U.S.A.[3]	19.9	26.5	26.2	26.0	25.0	24.5	25.4
U.K.	21.9	22.0	21.5	21.2	20.4	19.7	19.3
Federal Republic of Germany	22.8[4]	10.0	12.0	13.2	14.8	15.5	16.1
Other European countries(5)	23.2	31.8	29.6	29.0	28.8	29.1	27.9
Canada	4.9	5.6	6.9	6.8	6.3	6.1	5.8
Japan	7.3	4.3	3.8	3.8	4.6	5.1	5.5
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Figures taken from the 27th Annual Report of the Bank for International Settlements.

(1) Belgium and Luxembourg, France, Federal Republic of Germany, Italy, Netherlands, Sweden, Switzerland, United Kingdom, Canada, United States, Japan. These countries account for approximately 90% of world exports of finished products exclusive of those by the Eastern European countries, the Soviet Union and China.

(2) January-September 1956.

(3) Less exports of special categories.

(4) German Reich: share of present Federal Republic in 1937 exports of finished products may be reckoned at approximately 15%.

(5) Belgium and Luxembourg, France, Italy, Netherlands, Sweden, Switzerland.

The share of exports in the gross national product in 1957 was 17 or 18% -- if we include revenue from services, 21 or 22%. Compared with other Western European countries, such as Belgium and Luxembourg or the Netherlands, whose exports amount to as much as 40 to 50% of the gross national product, this is not outstandingly high. But if we consider that the 1950 figure was only 10%, it does appear that exports were a vital factor in expansion throughout the period.

On the other side of the scale, the Federal Republic's dependence on imports proved less than had originally been expected. The share of imports in the gross national product in 1957 was only 13.5%, and even including the amounts paid in services it was barely 18 %. So dependence on imports is no greater than that of self-sufficient France. Foodstuffs and industrial raw materials each account for about 30 % of German imports. One circumstance with an important bearing on imports of industrial raw materials is the fact that liquid fuels are only a minor item in German supplies of energy, and that, moreover, one-quarter to one-third of the consumption of mineral oil is covered from highly-subsidized indigenous oil extraction. It is true, however, that the share of liquid fuels has risen fairly steeply in the last few years, which will mean increased dependence on imports.

These, then, are the outstanding points about the expansion of foreign trade an payments. As regards the foreign trade policy behind it, the influence of the occupying Powers was greater and lasted longer than in the case of internal economic policy. The basic principles of Soziale Marktwirtschaft -- currency stability, the subordination of internal economic policy to this consideration, the progressive elimination of rationing and import quotas, the liberalization of foreign trade, the gradual discarding of currency restrictions -- these various principles were not all accepted at the same time and in full by the occupation authorities.

Shortly before the currency reform, a uniform D-mark rate of 30 dollar-cents was established, with the object of standardizing the multiple rates of exchange. This dollar parity remained in force until the devaluation of the pound in September 1949. The question whether the new mark should be devalued to the same extent as the pound, by 30.5 %, was settled by a compromise: the devaluation was limited to 20.6 %, which restored the pre-war dollar exchange rate of 0.238. This more or less accidentally established parity has continued up to the present time, and is defended as the right one by the Federal Government and the Bundesbank. This is disputed in some quarters, particularly since the currency debate in the autumn of last year. It is contended that the Federal Republic's continually strengthening unilateral position as a creditor country proves that the rate of exchange was fixed too low and does not take account of the discrepancy between German and non-German price movements. The Bundesbank's reply is that there is no object in altering the rate to the disadvantage of German exports simply because price movements in certain countries are more erratic than they are in Western Germany. Furthermore, it argues that the balance-of-payments surpluses for 1956 and 1957 were caused not so much by price disparities as by a drop in demand -

- in fact, by superiority on the part of German exports as regards choice of goods and delivery dates. It is conceded that the general trend in prices has had something to do with it too. Perhaps we get closer to the real reasons if we recall the order of priority adopted for the various economic objectives, and in particular the subordination of home expansion to the preservation of a stable currency, and hence also to the all-importance of foreign trade.

Such a currency and foreign-trade policy made it essential to liberalize imports as quickly and completely as possible, to switch from bilateralism to multilateralism, and to lower tariffs. The Federal Government grasped the implications quite early on and acted accordingly, though this was not always easy and sometimes downright dangerous. Its whole approach to foreign trade was subjected to much criticism of varying degrees of virulence, first from the occupation authorities, and later from its internal opposition. Again, the real foreign-trade situation was by no means always such as to favour the Federal Government's intentions. Twice, in 1949 and in the autumn of 1950, the country was faced with a payments crisis and the Government had to restrict, and even temporarily rescind, the newly-instituted freedom of importation. The fact that the liberalization gamble, as it has been called, did come off after all was due to a number of external factors as well as to the talent and ability of the gamblers themselves. The international rise in prices as a result of the Korean war, which involved the Federal Government in great difficulties in the autumn of 1950, ended rather suddenly, and the ensuing recession in, more particularly, the United States was a fairly short and minor one which did not seriously affect the expansion in world trade. The German payments crisis was overcome with the help of E.P.U., and as early as January 1952 the Government was able to reintroduce the liberalizing policy which had had to be suspended in February 1951.

Tariff policy would appear to have lagged behind liberalization as an element in foreign-trade policy, and even on occasion to have run directly counter to it. The new customs tariff introduced in October 1951 represented a fairly substantial increase over the tariff previously in force, which dated from 1902. Still, in comparison with other European countries, it was not prohibitive: it worked out at an average of about

20 %, which can hardly be said to be excessive. Moreover, when it was first introduced its incidence on trade exchanges was relatively slight. For the first year or two even business men hardly realized it existed, and the Government did not treat it to begin with as an instrument of foreign-trade policy. But the position changed during the great boom from 1955 to early 1957. The Minister of Economic Affairs found his stable-currency policy menaced, there seemed to be the danger that the export industry would cease to be competitive, and finally the bogy of inflation loomed up, which after their two bitter experiences, never fails to make the Germans' flesh creep. From then on tariff reductions were employed deliberately, as a means of curbing prices at home. However, it soon became apparent that this policy could be done so far and no further. The prices of finished products were climbing in the principal competitor countries too. There were growing signs of resistance on further tariff reductions by certain manufacturing industries. The value of low raw-material prices was lessened, up to the middle of 1957, by the rise in sea freight-rates, and as regards agricultural prices nothing that the Minister of Economic Affairs could say or do had much effect in face of the determined resistance of the Minister for Agriculture.

Before concluding this chapter, I should like to add a word or two on export incentives. The Federal Republic has undoubtedly been subsidizing its exports. But it is not true that this was done by exoneration of exports from turnover tax. This system is adopted in all European countries; it is paralleled by compensatory taxes on imports. The principle of taxation according to the country of destination has been applied, as regards turnover tax, pretty well everywhere. The arrangements allowing the exporter to deduct 3 % of his export turnover from his taxable profits, and a further 3 % for the purpose of building up a reserve, are rather a different matter. They really were definite export subsidies. But what their actual incidence was is almost impossible to calculate. Thex expired at the end of 1955 and were not renewed.

Similar practices were current regarding export credits, as they were in other countries. Thus there were credit facilities for individual exporters, and balance-of-payments credits by way of E.P.U. and bilateral Swings. The Central Bank provided strong support, particularly in regard to the second type. The details of the credits were important: they allowed the exporter reduced rates of interest, which was very much of a major consideration in view of the high rates of interest on commercial loans in Germany. This was done for the most part by means of official rebates on interest, amounting to subsidies. The individual small exporter also had the advantage of assistance from the Ausfuhrkredit Aktiengesellschaft, a banking institution whose lending capacity however probably at no time exceeded 1,200 million marks. Its main advantage lay in the long-term basis of its loans, which were for periods of up to four years: in point of fact only a small proportion of those it granted were for more than two years.

The second category of export credits was based on the Federal Republic's surpluses vis-à-vis the European Payments Union. The Bank deutscher Länder's credit balances with E.P.U. and with the clearing-agreement countries -- originally intended only to offset short-term fluctuations, since they are based on short-term deposits -- were also used more and more for the long-term financing of exports. Since Western Germany's payments surpluses with E.P.U. and the clearing-agreement countries were growing, there was no real reason, from the technical banking standpoint, why long-term loans should not be financed in this way with short-term funds. All the same, the Bank deutscher Länder was not very enthusiastic about it.

Personally, I consider the most effective means of promoting exports to have been the export credit guarantee offered by the Hermes-Kreditversicherungs-Aktiengesellschaft. This is a private credit-insurance company backed by substantial Federal guarantees. As in the British export credit guarantee system, the risk is covered by premiums, and in the same way the nature of the risks to be covered is spread fairly wide. Not only did this considerably reduce the risk to the individual exporter, but Hermes also provided its clients with a first-class commercial intelligence and credit information service. In the first few years, when the Federal Republic was poorly off for connections with the outside world and import quotas and currency restrictions were still impeding international trade, this company was a double asset: it supplied the information indispensable to every exporter, and it opened up access to foreign markets by helping exporters to overcome other countries' administrative barriers to importation. In this way, Hermes gave most valuable assistance to the export trade, and more particularly to the medium-rank and small export industries which have always been strongly represented in Germany.

Lastly, the London settlement of debts of February 27, 1953, helped to re-establish the links between the Federal Republic and the rest of the world.

The Federal Republic, its former enemies and Western Europe

The rapid expansion of the German economy since the end of the war and the currency reform tends to obscure the fact that the post-war reconstruction period lasted up to about 1955 and went through several very different stages. Immediately after the surrender, up to about 1946-47, the economic policy of the Western Allies vis-à-vis Germany was to a greater or lesser extent influenced by the Morgenthau Plan. The Germans themselves, at any rate those in responsible economic and political positions, quite realized that in the queue of applicants from all over the world Germany would have to come pretty well at the tail end. But it was a great piece of good fortune that the Western occupation authorities were so largely guided by the approach of such outstanding men as General Clay and High Commissioner McCloy. The first break in the solid wall of mistrust of Germany came in the course of the sharpening conflict between East and West, with its inclusion in the Marshall Plan. The financial assistance afforded Germany under this scheme and from various other sources was initially very considerable. If we draw up a balance-sheet over eight or ten years, the Federal Republic has actually made over a good deal more in restitution payments and deliveries than it received by way of foreign aid. But we cannot really express what happened in this form, for what was ultimately much more momentous than financial aid was the change in the Western Allies' political attitude to Western Germany.

Western Germany's second big break is linked with the names of two French statesmen, Robert Schuman and Jean Monnet. The plan which they announced in 1950 and put through in 1952 for the integration of the coalmining and iron and steel industries of Western Europe has had the same excellent effect on the Federal Republic's subsequent political and economic development as has, conversely, the reconstruction of the German economy on the Common Market. For the West German coalmining and iron and steel industries it meant the abolition of controls and restrictions, integration into a single common market and dissociation from a purely national economic policy. The significance of the Coal and Steel Community lies first of all in the intensification of trade among the six countries. Then again it has established close contact among the industries concerned, and moreover among a wide range of different quarters in the six countries. And finally, the Community was a "test-case" to establish the conditions, requirements and possibilities with regard to fuller integration in Western Europe; the experience gained in the Common Market for coal and steel formed the basis for the institution of the General Common Market, which has been in its initial operative stage since January 1 of this year. The main, though not the only means to this general integration is a Customs Union of the six countries, to be formed in 12 to 15 years' time. Another important feature is the common "economic orientation", which will be to begin with a signpost for the enterprises' own activities, but may later become a definite target of economic policy.

Western Germany will have a major contribution to make to this development. But since 1956/57 it has itself entered on a fresh stage. One of the most abundant sources behind its economic expansion -- the large supply of manpower, represented by immigrant workers, the increasing number of juveniles available and the reservoir of unemployed -- will from now on be less abundant. The number of gainfully-employed persons, which increased between 1950 and 1955 by more than three million, is estimated to increase between 1955 and 1965 by only about 2.4 million.

As the manpower potential is now fully utilized and there is less possibility of increasing it than there once was, wages are rising faster towards the higher level prevailing in the other Western European countries. Moreover, since 1957 the hours worked have been shortening rapidly. As I mentioned earlier on, the increase in the number of employed persons has had almost as much to do with the general economic advance over the past year as has the rise in productivity. Does this mean that economic advance in Western Germany will be slower from now on than it has been so far? Yes, undoubtedly it does mean just that. The real rate of increase in the national product between now and 1965 is estimated at 3.5 to 4 % per annum. So it will be only half what it was from 1950 to 1957, which was 7.9 % -- though of course, in comparison with long-term past trends it will still be high. In addition, we can reckon that in future the number of active-employed persons will account for 9 - 10 % of the growth of the national product, and increased productivity for approximately 33 %.

I should like to end my lecture by touching briefly on two points:

First, there is the question whether the forecasts I have just mentioned will prove accurate. That depends to a great extent on the future orientation of the German economy —that ist, on whether it concentrates on domestic or on foreign trade. Well, the Germans being what they are, exports will always be a major priority in economic policy. As a matter of fact, the forecasts are that exports will represent over 20 % of the national product. For a big country like the Federal Republic that is even more important, but at the same time harder to achieve, than for smaller countries like Belgium and the Netherlands. Western Germany's export capacity is conditioned, among other things, by the elasticity of demand for its export goods. On the whole this is high — that is, demand reacts strongly to changes in relative prices. So if the advantages which the Federal Republic has so far derived from its lower wage-level are in future to diminish, it will be necessary to ensure a steep rise in labour productivity. At the same time, this will from now on depend more than it used to on capital equipment. The capital output ratio has up to now, as we have seen, been comparatively low, but it will have to be adjusted more and more to those of the other Western European countries. The prospects of achieving this are at present not too poor. The marked increase in savings in the first half of this year and the high degree of liquidity of the banking system have enabled enterprises to increase their own capital by issues of shares. Issues of industrial bonds have increased even more considerably, which has made it possible to consolidate previous short-term borrowings.

The other important question is in regard to the parallel development of the six countries in the Common Market. It is estimated that the annual rate of increase in gross national product of the Community up to 1965 will be about 4 %. That works out at an increase of 48 % over ten years, with the contributions of the individual countries varying between 30 and 60 %. Western Germany with its large currency reserves seems naturally destined to make a large contribution. How all this is to be achieved depends on the co-ordination of the individual Governments' economic policies. It is all very well to state this as a challenge, but as soon as we get down to technical action, ...

we find ourselves faced with a number of matters which seem, to begin with, to involve only difficulties and not much prospect of solution. Take the policy of the Central Bank, take the policy on trade with third countries, take agricultural policy, and so forth. All those are questions I cannot go into now.

To sum up, two points seem to me well worth putting on record: German reconstruction was an experiment as to the validity of the neo-liberal approach. It was unquestionably a success. Whether it would have been a success in any circumstances, and whether it can be brought off again, is a great deal more problematical. We must not forget -- and this is my second point -- that external factors also operated in the Federal Republic's favour. Success was not unconnected with the conflict between East and West, with the Western Allies' general attitude of benevolence towards Western Germany, and, it seems likely, also with long-term trends in the world at large.

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