it is not altogether improbable that further developments may be anticipated in this field.[1]

In the private sector of the economy, the release of the accumulated demand for durable goods has tended to obscure the long-range picture. Looking to the future, it would appear that, once replacement and maintenance programs have been reduced to a more normal size and capital investment in plant construction begins to taper off, Canada will have a substantial surplus capacity for the production of durable goods. Although many products in this category would be strongly competitive in the export market, ability to compete is not in itself the decisive factor in a world where international trade has not been re-established on a multi-lateral basis. Eventual recovery in Western Europe implies a marked increase in that region's production of durable goods for domestic and foreign markets. In the United States, as in Canada, increasing attention will be given to exports as the backlog of domestic demand is reduced, thus adding to the difficulty of marketing Canadian goods abroad.

The post-war program of capital investment in modernization and expansion of existing production facilities has tended to correct the temporary imbalance which had resulted from the intensive development of selected industries during the war. To-day the efficiency of Canadian manufacturing and its potential output are at higher levels than ever before. In terms of markets, the position is relatively strong for the present and probably for the immediate future. But overshadowing the problem of future consumption capacity in the home territory is the riddle of prospects for foreign markets. The achievement of multilateral trade and of more stable international conditions is essential for sustained prosperity in Canada.

1. At p. 234 of this issue, the significance of the iron and steel industry and its problems is discussed by M. Hollinger in "Steel—The Key to Industrial Expansion."—Editor'.

The European Recovery Program

By Rodney Grey

THE first reaction of Canadians to the inauguration of the foreign assistance programme of the United States was the hope that our export and currency problems would be solved. It has now become abundantly clear that optimism was quite unjustified. From the very beginning, of course, government leaders like the Minister of Trade and Commerce, Mr. C. D. Howe, warned that ERP was no solution for Canada's U. S. dollar shortage, and that Canadian exporters would have to make even greater efforts to sell their goods in foreign markets as the post-war sellers' market declined.

EDITOR'S NOTE: Rodney Grey, B. A. (Queen's), M.A. (Toronto) is Assistant Financial Editor of *Saturday Night*.

In addition to ERP, of course, there are other important factors affecting our trade pattern. The major development since ERP was launched is the American rearmament program. Purchases of materials and supplies in Canada may provide a solid floor under our drive for increased exports to the United States. A good deal of such purchasing would tie in with the production of war goods which would be lend-leased to European nations. In the strictly military sphere, this armament scheme is the counterpart of ERP's objectives in the civilian sector of the European economy. Until further policy decisions have been announced, however, its implications for Canadian industry cannot be assessed.

In the first half-year of ERP Canada has received about twenty per cent of total spending by the Economic Co-operation Administration of Paul Hoffman in Washington. There are several reasons why we got such a high proportion of initial expenditures. Perhaps the most important is that we had the goods that European countries needed, and we had them at competitive prices. Canadian government officials — trade commissioners, and officials of all departments concerned at Ottawa—did a good job of selling Canadian goods. They got the information on quantities available and prices to officials in Washington and to government purchasing agents in Europe. Also, we had already many valuable contracts with the sixteen nations that share ERP funds: ECA simply underwrote these contracts. Instead of European countries digging into scanty reserves of U.S. or Canadian dollars to pay us for our wheat, dollars were forthcoming from the Economic Co-operation Administration, to honour these outstanding commitments. And lastly, a major reason as yet little appreciated in Canada, is that the first half-year of the European Recovery Programme demanded just the sort of bulk raw materials and foods that Canada has always supplied to Europe. One of the very specific provisions in the Foreign Assistance Act is that it must not break up already well-established trade patterns. We have always sold those sorts of things to Europe and it was easy to persuade the American officials that as long as those sorts of things were being purchased, they ought to be purchased in Canada.

Temporary High Spending

The first half year made many Canadian farmers, manufacturers and traders very happy. With a floor under our export market provided by ECA dollars, the future looked rosy enough. But these factors causing a high proportion of ECA spending in Canada are all of a temporary character; despite their operation, our trade to overseas areas has declined forty per cent this year from last year. What ERP has done is to prevent a very drastic deterioration of our export market; it has postponed the evil day of adjustment, and made it possible for us to make our trade reorientation more slowly. Despite ERP, we must sell more to the United States and to Latin America; we must be prepared to sell less to Europe and to the sterling area. The base of the trade triangle of the North Atlantic has been permanently shifted.

Canadian producers are faced with a period of major readjustment to this fundamentally changed market. ERP is a crutch that will help them along, but it is certainly not a total support. Not only are the temporary factors producing a high inflow of U.S. dollars in the first six months of ERP already on the decline, but there are other positive factors which will come increasingly to the fore as we enter the second half year.

There are five of these factors; it is impossible to estimate at this early date which of them will mean the greatest reduction of income from ECA. Certainly a major factor will be increased spending by the Economic Co-operation Administration in Latin America. Many countries in South America—the Argentine, Brazil, Chile—have ready for sale to Europe the same sort of things that we want to sell, and if they can meet our prices, they will find Europeans anxious to buy there. For obvious political reasons, inherited from the days of the Good Neighbour policy, Washington will be happy to have ECA dollars going to Latin America.

Soft Currency Spending

A second major factor that will reduce ECA purchases in Canada is the increased spending by European nations within the soft currency areas. Under UNRRA and under the American and Canadian loans to European countries, there was a certain amount of exporting of surpluses to Europe—it was our money, and we shipped what we had, sometimes, rather than what they really needed for reconstruction. The pressures to get unessen ial goods were certainly not exclusively European. However, now there is a sort of public examination of conscience in Paris when a nation asks to have purchases financed by ECA. Any country that wants to spend money from ECA must have the purchase cleared with the Organization for European Economic Co-operation in Paris; many other nations will complain if scarce U.S. dollars are being used for goods that can either be done without or can be bought within the soft currency area. That this should be so is fundamental to the foreign assistance program.

At the same time as European spending within the soft currency area is being revived by the pressure of collective opinion and the scrutinizing of Averell Harriman's staff at OEEC in Paris, some ECA dollars may well be diverted from purchasing goods in the New World to supporting currencies in Europe. One of the causes of the low level of intra-European trading has been the lack of a freely convertible currency within the European area—that is, a currency that would be accepted by countries for exports in the belief that they could buy goods with it.

Britain and Belgium, having gone further along the road to economic recovery than other nations in Europe, have been building up trade balances with their European neighbours. In order to help countries like Britain and Belgium, and they must be helped if European trade is to be revived, the United States is engaged in negotiations to set up what amounts to a European clearing scheme. Since originally suggested it has gone through a variety of changes, but the net effect is that fewer ECA dollars may be available for offshore purchases.

American Competition

Another reason, and in the future this may well be the main reason for reduced offshore spending by ECA in Canada, is that many Canadian products that we could sell to European countries are also produced in the United States. If there is a surplus of tobacco in the United States, for example, it is hardly likely that very many ECA dollars will be used to buy Canadian tobacco. U. S. producers will get the first chance to benefit from the expenditure of U.S. dollars. The pressure for economy in government —that is, economy of foreign spending —combined with the pressure from producer groups, already well-organized and vocal, ensures this.

One important section of the Foreign Assistance Acts states that when the Secretary for Agriculture declares any agricultural product to be in surplus supply, the Economic Co-operation Administration must buy that surplus if there is any demand for it by European nations. The Department of Agriculture pays half the price, ECA pays the other half. Both the administration of President Truman and Congress want to keep farm prices high. Canadian producers have no cause for complaint in the e provisions, but the net effect is that we may find it increasingly difficult to sell many agricultural surpluses in Europe.

These factors are all bound up together, but a further one that may be separated out for analytical purposes is the change in the sort of goods that Europe will require in the later stages of the recovery program. ERP in its beginning has been more of a relief program than a reconstruction program, but good crops this year in Europe combined with some stockpiling of foods and raw materials means that in the second half-year of ERP the emphasis will begin to shift from foods and materials to machine tools and other instruments of reconstruction. Canadian manufacturers are anxious to sell machinery in the world market (that means in effect in Europe), rather than being dependent on a small home market and a Commonwealth market steadily getting smaller because of United Kingdom recovery and sterling area dollar restrictions.

But Canadians are going to have to fight very hard to sell machinery to Europe under ERP. In some lines, of course, it may be easier than in other. The United States, faced with a shortage of farm machinery, has limited the amount that may be shipped abroad. The Canadian farm machinery industry, already operating in world markets, will, no doubt, get a good chance in the European market. But as far as complicated machine tools to put Europe's factories on a peace-time 1949 footing are concerned, Canadian producers are in a poor position. They will have to compete on prices with American producers, more soundly based on a large home market, with far greater research facilities, and much greater in size. The heavy industry of a country like Canada is bound to be at a disadvantage generally in producing highly specialized machinery.

In addition there are many complicated engineering problems to cope with, and the larger American industry is better equipped to solve them. Perhaps the greatest difficulty is standardization; the recent projected agreement to work out common threads and sizes for nuts and bolts is only a beginning in the enormous dovetailing of British and American industry, let alone integration with that of the Western Zones of Germany, with France, Belgium and Holland.

As well, Canadian industrialists who produce machinery and tools are tending to ignore the fact that the British heavy engineering industry has made a very good comeback from war conditions, and that it will be in a position to supply goods to Europe as ERP supports British exports to the continent. As far as this portion of ERP is concerned, while we may sell to Europe some products of our factories, Europe can hardly be a major market for this industry. The currency difficulties, coming on top of the natural disadvantage that Canada suffers in a world market for factory products, means that we are likely to be forced back upon the home market; we must tailor our plans for industrial expansion to the needs of the home economy. We would be unwise to think that the sellers' market for any kind of machinery is going to last very long, if it is not already over.

Canada's Prospects

All these factors added together mean that we must not expect too much from ERP. In a number of different lines, the failure to move goods to Europe with ECA funds is already evident. Our major export, wheat, is a good example. We have a crop higher than last year—391 million bushels, of which we have contracts for 140 million bushels with Britain. A good portion of what remains is a surplus, and it is becoming rather painfully evident to western wheat farmers and to officials in Ottawa, that if we want to sell that wheat we will have to finance it ourselves. The recent talks with Sir Stafford Cripps in Ottawa suggest that an extensive Canadian foreign aid programme is unlikely.

Tobacco is another example—our crop this year is above last year's—yet Britain, a big buyer of tobacco, has been forced by currency restrictions to purchase only $7 million worth. If any more is to be bought with ECA dollars, it will be American virginian tobacco, for producers of the American tobacco surplus are already putting considerable pressure on Washington to allow tobacco to be shipped with ECA authorization. Much the same story might be told of British Columbia and Maritime fruit and fish. In normal times we could hope to sell some in European markets, but overall currency shortages combined with the fact that American dollars will be used to buy American goods if available means that Canadian producers are being squeezed hard trying to sell abroad.

This listing of factors which will reduce our share of offshore purchasing or reduce our total exports to Europe makes a gloomy picture and it is safe to say that the prospects of a high level of trade between Europe and Canada depend, even while ERP is functioning, on our willingness to buy European goods and Europe's ability to produce goods that Canadian consumers will buy.

The conclusion cannot be escaped that the rosy optimism of the early months of ERP was not justified by events and that the prospects for the future are anything but bright. ERP is an attempt on the part of the United States to underwrite European recovery, to re-establish Europe as a part of the world trading economy, able to stand on its own feet financially, able to pay its way. Its purpose was not to solve, immediately, the export problems, of nations of the western hemisphere. Canadians are coming rather reluctantly to the conclusion that ERP has only postponed and eased the process of adjusting ourselves to a changed world market.

American Branch Plants and The Dollar Problem

By Donald A. Fergusson

THE movement of American "branch plants" into Canada has for long constituted one of the largest and most dynamic factors in Canada's industrial development. Without this movement Canada would undoubtedly have lagged far behind its present position among the industrialized nations of the world. However, Canada's productive achievements during the war years indicate that tremendous possibilities still lie ahead; for the war-time integration of her specialized productive capacities with those of the United States actually resulted in the opening up of an entirely new industrial frontier in this country.

More recently, exchange difficulties have threatened to prevent the full exploitation of these industrial possibilities, largely because Canada's European customers have been unable to provide the convertible exchange required to keep the traditional "trade triangle" in balance. Thus emergency measures have been necessitated to conserve American exchange.

In setting up and administering these regulations, there has been no intention of imposing drastic restrictions upon industrial development. The aim has been rather to promote industrial growth in the most constructive possible way by allocating the available American exchange to economically sound developments, i.e., those which later will be able to continue without the protection now temporarily provided by exchange controls. Even though the short-run consideration of United States exchange savings has been taken into account, particularly in the regulation of consumer goods imports, the guiding principle has been the improvement of our United States dollar position wherever possible through the expansion of production and exports rather than through the restriction of imports.

Thus, despite the exchange restrictions, the movement of new American branch plants into Canada, which continued to be one of the chief means by which her early post-war industrial de-

EDITOR'S NOTE: Donald A. Fergusson, M.B.A., is a Canadian now lecturing in finance at the School of Business Administration, University of California. In the past summer, he was with the Economic Research Branch, Department of Reconstruction and Supply, Ottawa.