SWITZERLAND AND STERLING.

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While clearly recognising the solid advantages to world trade bound to result from increased facility for effecting international payments, and from an ultimate recovery by London of its former function of world money-market, Switzerland is unable for the time being to agree to the proposal that she should join the group of countries ready to accept sterling to any amount, even from countries not belonging to the sterling groups, in the settlements of accounts arising in current business after July 15th, 1947. No formal negotiations have taken place between the two Governments but, an unofficial discussions of the situation in London, the attitude of Switzerland was made unmistakably clear.

But, as the reasons given showed, this decision was by no means the last word.

As matters stand, business between Britain and Switzerland is regulated by the Anglo-Swiss payments agreement of March 12th, 1946, valid until 1949, whereby Switzerland agreed to put at the disposal of Britain whatever amount in Swiss francs should be required for purposes of trade between the two countries. Up to the equivalent in francs of £15 million, Switzerland agreed to hold sterling. If Swiss francs over and above that limit were wanted, Britain undertook to place gold at the disposal of the National Bank of Switzerland. This has actually been done and the agreement has so far worked well.

No change in the arrangement would have occurred if Switzerland had agreed to provide francs on demand against sterling arising in current trade among countries belonging to the sterling group. But as there is a worldwide demand for Swiss francs, it is self-evident that — as the £15 million credit is now exhausted — Switzerland would constantly have to ask Britain to exchange sterling for gold. This would bring Switzerland no advantages whatever. Switzerland already has ample reserves of sterling and a superfluity of gold. But of the two she prefers gold. No assurance, however was forthcoming that Britain would be ready and able to convert sterling into gold promptly on demand as fast as current business might make that necessary. Moreover, under such an arrangement, the National Bank would be likely to lose all control over the note issue.

Before Switzerland could undertake to accept to any amount sterling arising in current business, the National Bank would have to be in a position to accept gold to any amount without embarrassment. Refusal to convert gold or dollars into francs to any amount on demand became necessary during the war as a safeguard against inflationary effects. This was due to the dislocation of trade. Normally, Switzerland has a heavy trade deficit, her balance of payments being kept in equilibrium by invisible exports in the form of tourist trade and the receipt of interest and dividends on her investments in other countries.

In the first six months of 1938, imports aggregated sFr.781 million, exports sFr.618 million, trade deficit sFr.163 milion. During the war, to keep her workers employed, Switzerland continued to export. But she was unable to import on the corresponding scale, partly owing to the scarcity of commodities, partly owing to her isolation. In the first six months of 1945, imports aggregated sFr.285 million, exports sFr.593 million, export surplus sFr.308 million. Switzerland was being depleted of raw materials and her reserves of food were running low. So that against the *increase* in the note circulation due to the conversion of gold into francs, there was a decrease in the quantity of commodities on the market, inflationary effects being inevitable. This is borne out by official records. In 1938 the note issue was sFr.2,290 million. In 1945 sFr.3,518 million, in 1946 sFr.3,633 million, in May 1947 sFr.3,908 million. The cost-of-living index (1914 =100) rose from 137 in 1938 to 209 in 1945 and 216 in May, 1947.

Nevertheless, business men, manufacturers and bankers in Switzerland are now almost unanimous in the opinion that the danger of further inflationary effects is past, so that now Swiss francs could be issued freely against gold to satisfy all current demands, more particularly in effecting the transfer of interest and dividende on Swiss capital invested abroad and even in the repatriation of Swiss capital itself. Up till now, however, the National Bank has resisted the demand for a relaxation of existing restrictions.

A vehement protest against the policy of the National Bank was made on behalf of Swiss industry when Dr. Walter Boveri, president of the board of directors of the worldwide concern Brown, Boveri & Cie, Baden, addressed the shareholders on July 15th. Dr. Boveri pointed out that in 1946 imports exceeded exports by sFr.747 million. Allowing sFr.240 milion, he said, for the earnings of the Swiss tourist industry, the Swiss balance of payments was negative by about sFr.500 million. " Still more impressive are the figures for 1947," he said. In the first six months of 1947 imports aggregated sFr.2,224 million, exports sFr. 1,593 million, deficit sFr.631 million of which sFr.217 million arose in trade with U.S.A. Earnings from tourism have not increased noticeably in 1947, so that the gold and dollars amassed in Switzerland in the last few years are now being rapidly reconverted into reserves of raw materials and food. This meant, said Dr. Boveri, that all the dollars now received in current trade are required immediately to pay for imports, so that "it is in the highest degree probable that ample cover for all dollars arising in financial transfers is already available." "If we continue at this rate," he added, "we shall use up our dollar reserves and very soon arrive at the time when our reserves will be too small. . . . Therefore it is already time for us to take all possible steps to attract gold and dollars instead of inventing complicated measures to repel them."

Dr. Boveri admitted that during the war there might have been some justification for the excessive caution exercised by the National Bank of Switzerland. "But it is essential to point out that the competent authorities themselves are no longer of the same opinion as then. This is evident from the fact that in the first five months of 1947 the Confederation redeemed loans and treasury bonds to the value of sFr.572 million, obviously without fearing inflationary effects from increasing the circulation to that extent."

Because of the maintenance of war-time restrictions, Boveri continued, there is in Switzerland a dual rate of exchange for the dollar—the official rate 4.28 to 4.31 at which all commercial transactions take place, and the "free dollar" rate 3.60 to 3.90 obtainable for dollars the National Bank will not convert into francs. Actually, the free dollarrate fluctuated around 3.83. In U.S.A. no distinction is made between the two kinds of dollars. To settle small accounts, anyone can buy dollar notes at a Swiss bank at about 3.80 and post them to U.S.A. Larger amounts are frequently taken from Switzerland to U.S.A. in traveller's luggage. No law either of Switzerland or U.S.A. is thereby violated.

Bankers, industrialists and business men are convinced that if the National Bank were to allow the free dollar to be used without restriction to pay for imports, as Dr. Boveri demanded, the duality of the rate of exchange would quickly vanish. If certainty could be obtained on that point, there would be no reason why the National Bank should any longer resist the demand for the removal of all restrictions. Switzerland might then be able to reconsider the proposal to join the group of countries ready to accept all sterling arising in current business, provided, as competent quarters point out, ample safeguards were provided.

In official circles, however, opinions about the probable movement of the two dollar rates after removal of restrictions, differ. If all restrictions vanished, all commercial payments would be made in free dollars. This would cause the present rate of exchange of the free dollar to rise somewhat. Applications to the National Bank for dollars at the official rate would cease. As vast amounts of free dollars will arise from the gradual release of Swiss dollar balances blocked in U.S.A. since 1941, the duality might persist for a long time. This would embarrass the National Bank which would have to go on converting dollars into francs at the official rate — 4.28 — without being able to sell a single dollar. In these circumstances, a demand would probably arise for an adjustment of the official rate to that of the free rate. This idea would be encouraged by certain interested quarters which have long advocated a revalorisation of the Swiss franc. Against this, however, both the Confederation and the National Bank have always opposed their entire authority. Revalorisation in other countries has led to regrettable consequences.

Both the Confederation and the National Bank are eager that the duality of the dollar rate should disappear. Both will do everything possible, short of abolishing all restrictions, to cause the free dollar rate to rise. If it became steady appreciably above 4.00, the risk involved in allowing the use of the free dollar to make commercial payments might no longer be considered great. But even under the most favourable circumstances, this is not thought likely to occur for several months.

To settle accounts with dollar countries, Swiss importers are obliged by present regulations to buy dollars from the National Bank. But there is nothing to prevent importers of raw materials in competitor countries from using free dollars to settle their accounts cheaply *If they can get francs to buy the free dollars.* If, while the present difference between the official rate and the free dollar rate exists, Switzerland agreed to join the group of countries accepting sterling freely, pounds would be converted into francs on a large scale by competitor countries to pay for purchases in dollar countries. This would obviously have serious consequences for both Britain and Switzerland.