of \$5.6 billion, at an annual rate, during the disastrous first quarter of this year.

Of the \$5.1 billion deficit of the last four years, about \$1.8 billion was financed by reserve losses and the liquidation of the foreign securities vested during the war by the U.K. government. The rest (\$3.3 billion) was financed by repeated borrowings from the IMF and foreign central banks, part of which was cancelled, in dollar terms, by the devaluation of the pound, last November.

Summing up the policy measures adopted by the U.K. to redress its situation (wage freezes, tightening of credit, restraints on capital exports, tax increases, reductions in government expenditures, devaluation of the pound, and, last but not least, the semi-consolidation of volatile sterling balances announced earlier this month) one can hardly avoid the feeling that the U.K. balance of payments should finally improve, drastically and rapidly. The still disappointing record of recent months certainly reflects continued distrust on the part of the so-called "gnomes" of Zurich and other places—including London itself. This may reflect in part the fact that the measures listed above were adopted only one at a time rather than grouped in a convincing and impressive package, and that the Government felt compelled each time to alarm public opinion by gloomy forecasts of the threats hanging over the pound, in order to justify each of these measures, none of which could, in isolation, be taken as an adequate remedy for the basic disequilibrium in the British economy.

5. *The surplus countries*

Large increases in the current surplus and net capital exports of other industrial countries (particularly the Economic European Community and Japan) have provided the main offsets to the deterioration of the U.S. and U.K. current account and capital exports.

The current account of these countries improved by about \$4.6 billion between 1964 and 1967, and their net capital exports increased even more, by \$5.9 billion, thus reducing their net reserve accumulation by about \$1.4 billion a year. Most of their reserve increases over these four years was accumulated in gold metal (\$3.9 billion) while their foreign exchange assets do not show any increase over the period as a whole. Their reserve lending to the IMF, however, rose spectacularly, by about \$2.6 billion, from \$2.2 billion to \$4.8 billion.

6. *Policy conclusions for the U.S.*

A. Our main efforts should clearly aim at a drastic improvement of our current account balance, enabling us to resume the normal level of net capital exports to the rest of the world which economic as well as moral considerations should lead us to expect from the richest and most developed country in the world economy.

Controls over capital exports should be eliminated as soon as the success of such a redirection of our present policies will permit.

B. A number of my academic colleagues consider that this recommendation should be implemented by a devaluation of the dollar, necessary to restore our price and cost competitiveness in the world economy. This view will undoubtedly prove correct if our price and cost increases continue at their recent pace. The GNP price deflator was rising during the first half of this year at an annual pace of about 4%. That this reflects mostly internal rather than external inflationary pressures is confirmed by the fact that our export prices—which reflect both domestic and external factors—are rising by only 3% a year, and that our import prices—determined nearly exclusively by foreign conditions—have not risen at all over the same period.

Yet, I would myself regard any dollar devaluation as premature, and strongly hope that we may still be able to avoid it through alternative policy actions. Indeed, in a full employment economy already subject to such inflationary pressures, a dollar devaluation—even if deemed acceptable at home *and abroad*—could only improve the current account at the cost of accelerating even further domestic inflationary trends.

We shall be unable to gauge correctly whether our prices and costs are still competitive or not before we have eliminated the overspending which is, at present, the major cause of both the inflationary overflow of dollars at home and the deficit-triggering overflow of dollars abroad. We must tailor down our overall rate of private and government spending to the GNP achievable in a full employment economy—or rather somewhat below, in order to restore the current account surplus needed to finance normal and desirable rates of capital exports and reserve increases.