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INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

LATIN AMERICAN GOLD AND DOLLAR HOLDINGS

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Economic Department
Prepared by: Antonio Dore
SUMMARY

1. From the end of World War II until the beginning of 1949 Latin American gold reserves and short-term dollar balances decreased by $900 million.

2. The trend was reversed during 1949. In that year those assets increased by $300 million, and in 1950 by $400 million.

3. While the increase in reserves in 1949 was largely due to import restrictions, the further increase in 1950 resulted chiefly from an improvement of Latin American terms of trade.

4. Both in 1949 and 1950, dollars accrued to Latin America not because of a direct current account surplus with the U.S., but mainly because of dollar payments received from European countries. Speculative movements of capital also are likely to have played a significant role in 1950, while the amount of U.S. new direct investment declined.

5. Although in the near future Latin American earnings from exports are expected to be high, the increased volume and value of imports will probably prevent a further substantial rise in Latin American reserves.

6. In general the past increase in reserves can be considered a favorable element from the point of view of creditworthiness. In the future, however, the use made by Latin American countries of their current high earnings will be a more important element in appraising their long-term creditworthiness than the level of their gold and dollar holdings.
LATIN AMERICAN GOLD AND DOLLAR HOLDINGS

From the end of the Second World War until the beginning of 1949, Latin America as a whole experienced a considerable drain on its gold reserves and dollar holdings accumulated during the war period. This was mainly the effect of the high volume of imports from the United States which in 1947 reached a level four times higher than in prewar. Large trade deficits with the U.S. developed, despite the considerable volume of Latin American exports and the improved terms of trade compared with prewar years. During the same period, Latin America had current account surpluses with the non-dollar area. But only a minor portion of the proceeds earned through these transactions - insufficient in any case to balance the total current account of Latin America - could be used for financing the deficit with the United States. The result was a decrease in reserves amounting to some $900 million.

Despite this decline, gold and dollar holdings of most Latin American countries - with the marked exception of Argentina - remained well above their prewar level. Contrary to the general trend, Venezuela and Cuba continued to increase substantially their international reserves throughout this period.

In order to prevent a further loss of reserves, in 1947 many Latin American countries started to introduce trade and payment restrictions. These restrictions were mainly responsible for reversing the downward trend and for making possible a net accumulation of Latin American gold and dollar holdings which began in the second quarter of 1949. The increase in these assets during 1949 amounted to about $300 million. Gains of individual countries varied according to local conditions and to price movements of international commodities, such as the increase of coffee and the decline of copper prices. The unequal distribution of ERP offshore procurements in Latin America also played a major role. The flow of private long-term capital from the U.S. was particularly high during the year, due mainly to large direct investments of the oil companies in Venezuela.

Another important aspect of the postwar years was the fact that most Latin American countries showed net gains in their trade with Europe, reflected first in an accumulation of sterling and soft currencies, and then in net dollar receipts from Europe, partly drawn on European-owned reserves and partly acquired through ERP-offshore purchases. In 1946, liquidation of direct investment, such as the sale of British railways in Argentina, was another substantial source for covering the European postwar deficit with Latin America. And to the extent that such sales went to settle previously incurred European liabilities, they facilitated current transactions.

This situation represented a departure from the pattern of international economic relations existing in the prewar years, when most Latin American countries, with the exception of Argentina and
Uruguay, were current account creditors of the United States and current account debtors of Europe. Since then a large share of Latin American trade has been absorbed by the United States, which was a market for exports during the war and has been a source of Latin American supplies thereafter, while Europe was still recovering from the economic disruptions caused by the war. A trend towards a bilateral balance was expected with the increase of European production and the rapid depletion of the extraordinary sources of financing in both Europe and Latin America.

In 1949, in fact, Latin American exports to Europe (mainly Argentine and Brazilian exports to the U.K.) declined sharply with a consequent narrowing of the Latin American export surplus with Europe. And in the first quarter of 1950, when current account transactions with the United States were approximately in balance, no net transfers of dollars from other areas to Latin America seem to have taken place.

Although this bilateral balance resulted mainly from curtailment of Latin American imports from the United States and lower prices or price resistance for Latin American exports to Europe, the effort made by European countries to regain their prewar position in the Latin American markets was considerable and to a certain extent successful, particularly after the devaluation of European currencies in the fall of 1949. It was partly aided by the restrictions enforced by Latin American countries against imports from the United States. But changes in the structure of Latin American trade made this effort difficult. The composition of Latin American imports had changed as a consequence of government controls tending to increase the share of capital goods imported in relation to consumer goods. Moreover, the economic expansion in the Northern part of Latin America, an area which is structurally more dependent on trade with the United States than with Europe, was more pronounced than the expansion in the Southern part of the continent, which customarily had been a more important market for European exports. The volume of trade of Argentina particularly, Europe’s principal trade partner in Latin America, did not rise from its prewar level and her capital goods imports increased only at the expense of other types of imports; finally, the virtual disappearance of Germany from world markets practically until 1950 had a considerable effect in shifting a part of the Latin American trade from Europe to the United States. In prewar years Germany had accounted for almost 50% of total European exports to all Latin American republics, excluding Argentina.

In addition to these changes in the trade structure, the current account transactions of Latin America vis-à-vis Europe and the United States were affected by the lower level of dividend and interest payments to Europe and the higher receipts of the United States as a consequence of the contraction and expansion of European and American investments, respectively, in Latin America.
The bilateral balance achieved in the first quarter of 1950 by Latin America with both Europe and the United States might have suggested a first step toward the re-establishment of the prewar relationship in dollar payments between the three areas. This seems to be the condition for a stable solution of Latin America's international economic relations, but the bilateral balance was not maintained in the remaining part of the year. The improvement in the terms of trade of Latin America with industrial countries, together with capital movements, gave rise again to net dollar receipts of Latin America mainly from Western Europe, and apparently despite the continued increase in the volume of exports to Latin America from European countries.

In the meanwhile, relaxation of payments and trade restrictions once more caused deficits on current account with the United States in the second and fourth quarters of 1950. For the full year—although Latin America achieved a substantial export surplus in its trade with this country for the first time since the end of the war—the deficit on service account was larger than the trade balance surplus by $271 million. The increase of some $400 million in Latin American gold and dollar holdings in 1950, which actually took place entirely during the second half of the year, did not result therefore from a current account surplus with the United States. Factors which contributed to the increase of these assets were: net dollar transfers from areas outside the United States, which represent partly an inflow of speculative capital rather than dollar payments for current account transactions; and a new flow of short-term capital from the United States, which was also largely of a speculative nature. The total amount of U.S. long-term capital invested in Latin America continued to increase in 1950, although at a sharply reduced rate after the virtual completion in 1949 of the oil investment programs in Venezuela. Gold reserves were further increased by government acquisition of a part of domestic gold production.

At the end of 1950 the gold reserves and short-term dollar assets of the Latin American Republics as a whole were again nearing the level attained by the end of World War II. Although these reserves were three times higher than before the war in terms of current dollars, the increased prices of Latin American import goods reduced the purchasing power of these assets so that at the end of 1950 their value in real terms was approximately 40% lower than in June 1945, and only 70% higher than in December 1938.

In the first months of 1951 Latin American gold and dollar holdings increased again by a further substantial amount.

From the point of view of creditworthiness, the recent strengthening of reserves of most Latin American countries is obviously a favorable factor, especially in regard to credits of short-term maturity. In evaluating creditworthiness for long-term loans, other factors
are of equal if not greater significance.

Limiting our analysis to the effects of increased reserves on the long-term credit outlook, some qualifications must be introduced regarding the nature of the present stronger reserve position. Whether this increase was the result of a predetermined policy or whether it was caused by the normal time lag between the increase in earnings and a subsequent increase of purchases, has an important bearing on the appraisal of long-term creditworthiness.

It is certain that in 1949 the strengthening of reserves was mainly the effect of a determined effort on the part of certain Latin American governments to limit their purchases abroad. In 1950 the increase in earnings was mainly due to external factors and in some cases the reaction of these same governments was to relax previously imposed restrictions. However, uncertainties about the future, the desire to strengthen the currency, and difficulties in obtaining certain types of goods from abroad, tend to lengthen the lag between rising exports and increased imports. At the same time the terms of trade of Latin America are bound to remain relatively favorable for quite a while since the demand for primary products in industrial countries is expected to remain at a high level.

Although any general conclusion should be qualified in relation to specific countries, it appears unlikely that Latin America will want to use its continued high current earnings to further increase reserves by substantial amounts in the near future, in view of the rise in import prices which occurred after World War II. On the other hand, a higher level of reserves could better cope with emergencies arising either from a sudden decline of the external demand for primary products, or from unexpected need for imports during the implementation of a development plan. Fears based on the recent postwar experience and import demands arising in an inflationary environment may lead to a dissipation of reserves. Should supply difficulties become more acute, the problem will be merely postponed; only appropriate internal measures will assure effective use.

At the present time, many Latin American countries already have a more or less satisfactory level of reserves. Therefore, the use which they will make of their current high earnings, rather than the change in the level of gold and dollar holdings, will become the most important element in appraising their long-term creditworthiness.
### Latin American Republics: Estimated Gold Reserves and Official and Private Short-Term Dollar Balances, 1938 and 1945-51

(In millions of dollars)

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<td>357</td>
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<td>463</td>
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<td>66</td>
<td>73</td>
<td>81</td>
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<tr>
<td>Uruguay</td>
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<td>377</td>
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<tr>
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<td>216</td>
<td>464</td>
<td>516</td>
<td>455</td>
<td>462</td>
</tr>
<tr>
<td>Other (45)</td>
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<td>515</td>
<td>594</td>
<td>756</td>
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* Data for official dollar balances alone are not available. The figures shown in the table include dollar holdings of central banks and other official institutions, commercial banks and private non-banking firms and individuals. Changes in private holdings, however, are believed to be relatively small. From January 31 to December 31, 1950, dollar balances of private non-banking firms and individuals of the above selected countries increased by $7 million (or 2%), while dollar balances of official institutions and commercial banks increased by $207 million (or 33%).

1/ Of which: gold $708 million and dollar balances $255 million. The country figures, shown in parenthesis, pertain to gold holdings only.

2/ Tentative estimate.

3/ $991 million including estimate for Uruguay.

Sources: National Advisory Council - Semiannual Reports to the President and to Congress.
IMF International Financial Statistics.
Export-Import Bank, Semiannual Report to Congress for the period July-December, 1945.