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A "blank cheque"? Portuguese World War II sterling balances, 1940-1973

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The perception that the loss of traditional markets had led to a weakening of the bargaining power of most neutrals led to a British move in 1939-1940 to negotiate payments agreements.[2] Besides killing off the free market in sterling centralized payments of British purchases in such markets coupled with British export controls would assure that Great Britain would be financed by neutrals at least for the duration.[3] With the U.S. Lend Lease it was of vital importance to finance the British war effort. The total sterling balances of £ 3,355 million do not compare too unfavourably with the £ 5,504 million that corresponded to transfers under Lend-lease net of Reciprocal Aid.[4]

In late 1940 an agreement was signed between the Bank of England and the Bank of Portugal on payments between the Sterling Area and the Portuguese Empire in line with other payments agreements signed by the British with neutrals in Europe and elsewhere. All sterling payments due to Portugal were to made into a special account of the Bank of Portugal in the Bank of England. There were reciprocal dispositions regulating escudo deposits in the Bank of Portugal but these had no practical importance.

The agreement was part of the British overall successful effort to kill the market for free sterling but "it was not by original design that [Portugal] became the holder of a substantial sterling balance."[5] The combined result of this agreement with the dwindling supply of British exports to Portugal and the surge in British expenditures in Portugal related to the war effort – with a crucial role played by wolfram pre-emptive purchases -- was the accumulation of large sterling balances by the Bank of Portugal. By August 1945 they had reached £ 76 million.

While the Portuguese balances corresponded to only about 2.3% of total sterling balances, both as a proportion of GDP or of Portuguese exports Portugal was in the same group of those economies that were directly affected by war operations such as Egypt and

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[1] This is a preliminary version not to be quoted. The author thanks the research assistance of Vitoria Rabello de Castro. Version dated 22.11.11.

[2] Accumulation of sterling balances in the Sterling Area by India and the Middle East -- Egypt, the Sudan, Palestine, Iraq, especially -- resulted from decisions on shared defence expenditures. See Sayers (1956), chapter IX.

[3] Keynes thought that the British bargaining position was "almost infinitely strong" as "there is the prospect of a hideous unsold surplus and market collapse" affecting raw materials. Minutes 12th Meeting Inter-Departmental Committee on Central and South America, 27.6.40 and undated Treasury minute of a letter to Khan, T160/1143 and Keynes´s paper on Foreign Exchange Control and Payments Agreements, 29.7.40, FO 371/24200.

[4] See Sayers (1956), p. 439 on comparative estimates of total sterling balances and pp. 531 and 535 on net Lend-lease. The net Lend Lease estimates do not take into account the US$ 650 million British repayment over 50 years

[5] Sayers (1956), p. 452.

the Sudan, the Palestine, and especially India, which held almost a third of the total balances. While from the point of view of Britain the Portuguese agreement had some importance – which increased until 1944 especially because of strategic imports -- from the point of view of Portugal the sterling balance issue was crucial.[6]

The case of Portugal is of interest also because, in contrast with other economies holding sterling balances -- such as those in South America -- there were no British assets in Portugal whose disposal could contribute to reduce or cancel the outstanding sterling balances in the negotiations after the war. Other solutions had to be devised and negotiated and they would have significant long-term consequences. To some extent the disposal of Portuguese sterling balances had some similarities with the case of India as even after transfers related to military stores, pension annuities (and previous redemption of sterling-denominated debt) Indian sterling balances remained extremely significant well into the 1950s.

1. Towards a payments agreement

After the outbreak of the war there were many frictions between the Allies and Portugal concerning economic blockade and foreign exchange matters. Most of the difficulties concerning the economic blockade were related to the limitation by the British authorities of exports to certain neutrals to their 1934-1938 average level as well as restrictions on re-exports using imported inputs. Portugal resisted these British proposals for a war-trade agreement until the fall of France.[7]

With the German occupation of France and the entry of Italy in the war blockade issues became even more crucial. It affected the position of Portugal as it became possible to export to Germany by land. Portugal became an adjacent neutral as opposed to overseas neutrals which were separated from the enemy by seas under British control. In July new legislation was introduced by the British authorities to apply rationing to Portugal and Spain and in the end of the month navicerts – commercial passports granted to approved cargoes by the British authorities -- became compulsory for imports while exports required certificates of origin.[8]

Portugal played a constructive role in the British effort to contain German influence in Spain as Salazar agreed to act as an intermediary to approach Madrid. The British offered wheat supplies and to allow the export of Portuguese colonial products under a United

[6] The accumulation of sterling balances was almost six times the German payments to settle the wartime balance of payments bilateral deficit of Germany with Portugal, see Valério, Nunes, Bastien, Sousa and Costa (2010). It is interesting to note that there is no reference to Portugal in contrast with other less important holders of sterling balances in any of the relevant official histories of the Bank of England, either Sayers (1976) or Fforde (1992), or in Schenk (2010) on the decline of sterling. The early negotiation of the agreement on the long-term liquidation of sterling balances in August 1945 has led to some confusion with the negotiations of the Monetary Agreemnt of 1946 regulating post war imbalances in the Anglo-Portuguese trade.
[7] Selby to Tovar, 16.11.39, 458/52/39, enclosure no. 314; Tovar to Monteiro, Ofício no. 9, enclosed aide mémoire on meeting with King, 29.1.1940 and Salazar to Portuguese chargé in Stockholm, tel. 16, 6.10.39.
[8] See Meddlicott (1952), chapter XV and Rosas (1990), chapter 1.

Kingdom-Portugal-Spain deal using the Anglo-Spanish Payments agreement signed in March 1940. A tripartite agreement was the basis for an exchange of notes of 27.7.1940.[9]

The sharp devaluation of sterling in relation to the U.S. dollar after the beginning of hostilities had led to the pegging of the escudo to the US dollar in November 1939 at 27$50.[10] As part of the effort to end the free sterling market and market the British authorities wanted to kill the market in free sterling which flourished in Lisbon but they were also pondering on whether Portugal "would not be prepared to lend us our adverse balance". [11] But there were worries about the possibility that Portugal would divert supplies to Germany.[12] After the payments agreement was signed the escudo-sterling exchange rate was stabilized at 100$000/£ reflecting the stabilization of the sterling-US dollar exchange rate. .

Negotiations of a payments agreement dragged between May and November 1940. The Portuguese wished to have a guarantee that their credit after the end of the war should be settled in gold three months after the end of hostilities but the British stuck to the position that if they insisted "they would control [British] imports so as to make such gold transfers insignificant".[13]

A payments agreement between the Bank of England and the Bank of Portugal was signed in 20 November 1940. The Bank of Portugal would open a Special Account in the Bank of England where all payments due in sterling by Portuguese residents would be made. Similar special accounts would be opened by Portuguese banks with their correspondents. The Bank of England would open a symmetrical account with Bank of Portugal. Both accounts would carry a guarantee based on the official price of gold of 168/6 per fine ounce. Amounts above £50,000 could be transferred to a Money Employed Bank Account "to be applied at interest by the Bank of England". [14]The agreement would remain into force until three months after the conclusion of the hostilities. Gold delivery in settlement of balances would take place as soon as "circumstances permit" and within five years after the end of the agreement.[15] The Portuguese gold clause was in line with those included in other payments agreements signed in this period which also included

[9] Tovar, memos on meetings with Eccles, 14.5.40 and 15.5.40, **Dez anos**, vol. XIV, pp.233-6; British Embassy, memo to Salazar, 23.5.40, **Dez anos**, vol. XIV, pp.240-1; Salazar to Spanish Ambassador in Lisbon, 24.7.40, **Dez anos**, vol. XIV, pp. 263-6.

[10] Salazar to Monteiro, tel. 323, 14.11.39, **Dez anos,** vol. XIV, pp. 94-5 and ofício 11, 14.11.39, **Dez anos,** vol. XIV, pp. 96-8.

[11] Playfair minute, 9.6.40, T160/1379.

[12] David Eccles worried: "There is a grave danger in encouraging an adjacent neutral to think that we know we can´t sell as much as we shall buy. They will then turn to Germany and sell to her rather than pile up useless sterling.", Eccles to Playfair, 1.7.40, T160/1379.

[13] Treasury and Bank of England to Ellis-Rees, tel .584, 29.8.40, T160/1379.

[14] In early 1942 the Bank of England agreed that sums in this account exceeding £ 5 million would be applied in the purchase of British Treasury Bills and still carry a gold guarantee, Norman to Governor Bank of Portugal, 13.2.42, BOE: C92/40..

[15] Agreement and Supplementary Agreement between the Bank of England and the Bank of Portugal, 20.11.1940, **Dez anos**, vol. XIV, pp. 346-51. The precise terms of the agreement remained undisclosed and were not reported in the annual reports of the Bank of Portugal see Leite (1946), pp. 37-8.

gold set aside or gold revaluation guarantees: Argentina, Brazil, Uruguay, the Nitrate Corporation of Chile, Sweden, among others.[16]

2. The accumulation of sterling balances

Portuguese worries with the future bilateral balance of payments made them press for a British note of the same date the agreement was signed that expressed the "desire of [HM´s Government] to respect the principle of balancing such exchanges so as far as possible to avoid the accumulation of balance in favour of one country or the other."[17] Anxiety was more intense in the Ministry of Foreign Affairs than in the Bank of Portugal where it was said that even if sterling balances reached £ 20 million a way would be found to reach a settlement.[18]

In 1942 and 1943, as Anglo-Portuguese relations became tense in the wake of questions related to supply of goods to Portugal, Salazar repeatedly mentioned the possibility of reviewing the payments agreement.[19] British alarm in 1942 prompted consideration of the convenience of arranging a visit of Keynes to Lisbon and "try the experiment of the power of his seduction on the Doctor" but it was decided not to promote it as it would make too clear to the Portuguese the importance attached to the issue by the British government.[20]

British doubts on the Portuguese willingness to accumulate sterling were recurrent until the end of the war. In mid-1942 reports that "the Portuguese would be unwilling to accept more sterling unless they receive what they consider an adequate supply of goods" were discounted as a bluff. [21] One year later there were again worries on whether the situation was not "too good to last indefinitely and whether Portugal might not cry "halt"". They were tied to worries on whether Portugal "in continuing to hold these substantial balances, [might not place] us under an obligation from which they can expect to derive present or post-war concessions from our part."[22] But, as it became increasingly clear that the Allies would win the war, the Portuguese appetite for sterling would prove to be insatiable.

British payments to Portugal more than trebled during the war in relation to its 1939 level – from about £8 million to an average of £26 million in 1941-45 -- while receipts stagnated under £ 10 million (see table 1). Portuguese sterling balances rose rapidly with

[16] Sayers (1956), p. 448.
[17] British note, 20.11.40, enclosed to Tovar to Bank of Portugal, ofício 46, 20.11.40, **Dez anos**, vol. XIV, pp. 351-2.
[18] Ministry of Foreign Affairs, memo on the trade balance with England (sic), 3.1.41, **Dez anos**, vol. XIV, pp. 384-6 and Eccles to London, tel . SAVING no. 7, 15.1.41, T160/1198.
[19] Ministry of Foreign Affairs to British Embassy, Note 181, 18.4.1942, **Dez anos**, vol. XV, pp. 133-4; Salazar to Monteiro, tel. 327, 18.9.1942 **Dez Anos**, vol. XV, pp. 186-7; Memo on Salazar-Campbell-Fisk meeting and British Aide Mémoire britânico, 12.6.1943, **Dez anos**, vol. XV, 335-40.
[20] Eccles to Makins, 30.4.42, FO371/31124.
[21] Waley to Casady (US Embassy), 12.5.42, BOE: OV6-213 and Turner to Cobbold,, minute, 8.6.42, BOE:OV6/214.
[22] Note (Wyatt) on Payments Agreement, 9.8.43, T160-1380 and Harmer to Wyatt, 18.8.43, T160/1380.

yearly increases reaching a peak in 1942-43 with an average monthly rate of increase of about £1.5 million.

The share of exports to Britain in total Portuguese exports rose from 20.6% in 1938 to a peak of 30.5% in 1943 while the share German exports almost doubled from 13% to 24.4%. The combined exports of wolfram and fish products rose from 18.7% of total Portuguese exports – mostly fish products – to about 43% in 1942 and 1943. Pre-emptive purchases of wolfram played a crucial role in the steep accumulation of sterling balances especially up to 1943.[23] The importance of wolfram had been enhanced by its use not only for lamp filaments, steel-cutting tools and catalysts but also in tank armour and anti-tank armour-piercing shells.[24] Pre-emption became especially important after mid-1941 as the German invasion of the USSR interrupted the supply of Chinese wolfram. Imports of non-ferrous metals rose to more than 60% of British total imports from Portugal.

Portugal´s aggregate export prices rose spectacularly as wolfram prices were on average almost 29 times higher in 1942 than in 1939. The selection of weights affects crucially the results as the share of wolfram in total exports increased until 1942 and then fell. After mid-1944 wolfram exports ceased entirely. Using 1939 or 1945 weights export prices increased between 154.7% and 181.9% in relation to 1939. But if 1942 weights are used average export prices increased by almost 1300% in relation to 1939.[25]

There were recurrent doubts in London on whether the pre-emption of wolfram was justifiable given its high cost, especially in Spain as the prices were much higher than in Portugal: £ 7500-8,000/ton compared to £ 1500 in Portugal and £300 in the world market.[26] But in spite of misgivings by the Bank of England and the Treasury pre-emption was maintained even if the Chiefs of Staff felt that they could not insist if financial arguments were powerful enough.[27]

In answer to early British pressure to block wolfram exports to Germany Salazar commented that if the German need for it was so acute as mentioned by the British an export prohibition would leave only open the alternative of the Germans coming to

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[23] Valério (2005).and Mateus (1999). For wolfram and the Portuguese economy during the war see Telo (1991), chapter X, Rosas, Martins, Amaral and Rollo (1994), and Nunes (2010). For wolfram pre-emptive purchases see Gordon and Dangerfield (1947), chapter VII, section 3. For wolfram generally see Li and Wang (1943). and

[24] War Cabinet Chiefs of Staff , memo on Wolfram, 7.6.43, CAB211/507.

[25] These export price indices have been computed for this article using raw data from Rosas (1990), p 148.

[26] Wheeler (1986), pp.118-9 and War Cabinet Chiefs of Staff , memo on Wolfram, 13.7.43, CAB121/507. The share of Iberian output of wolfram ores in the total world output reached a peak of 18.9% in 1943. Spanish output which was negligible in 1939 reached 60% of the Portuguese output in 1943, Smithells (1952) quoted by Caruana and Rockoff (2003). On Spanish wolfram see also Thomàs (2020).

[27] Cherwell, minute to Churchill, 19.11.41, CAB 121/503; Dalton, minute, 17.11.41, CAB 121-503; Cobbold to Waley, 23.3.42, BOE: OV6/213; Eady to Cobbold, 19.7.43, BOE: OV6/136; Jacob, minute to Churchill on Wolfram, 19.7.43, CAB121/507; MEW, note on Pre-emption of Wolfram, 21.8.43, T160-1276. The complexities of evaluating the impact of wolfram pre-emption on the German war economy are considered in Caruana and Rokoff (2003)..

Table 1
Portugal: Balance of Payments with the Sterling Area, 1939-1945, £ million

	1939	1940*	1941	1942	1943	1944	1945
Payments	7.6	4.5	20.8	29.1	29.0	27.5	23.1
Total UK	4.8	3.1	14.0	21.2	21.9	20.0	15.3
UK imports	3.7	1.7	11.1	14.0	12.8	11.0	8.8
Fish	0.3	0.8	2.5	1.6	2.7	3.3	4.3
Non-ferrous metals	0.2	0.1	3.5	9.2	7.2	4.7	0
Diamonds	…	…	0.9	0.8	1.7	1.6	1.4
Other raw materials	3.2	0.4	1.5	1.4	0.7	0.5	1.7
Other	…	0.4	2.7	1.0	0.5	0.8	1.4
UK invisibles	1.1	1.4	2.9	3.5	4.0	1.8	1.7
Allied governments	…	…	0.7	3.0	3.9	1.4	0.1
Other	…	…	1.2	0.7	1.2	5.8	4.7
Total rest of Sterling Area	2.8	1.4	4.9	7.9	7.1	7.5	7.8
Trade	0.7	…	…	...	6.4	…	…
Invisibles	2.1	…	…	…	0.7	…	…
Receipts	9.4	1.0	6.2	10.2	10.8	9.8	9.5
UK exports to Portugal	5.3	0.5	3.0	2.1	2.7	3.7	4.2
UK exports to Empire			0.7	0.8	0.5		
Freights	0.5	0.1	0.8	0.7	0.9	1.2	0.8
Interest and dividends	1.1	0.2	1.4	1.4	1.4	1.7	1.7
Service Departments			0.8	1.2	1.8	0.7	0.7
Rest of Sterling Area	2.5	0.2	2.0	1.5	1.5		
Trade	1.7					1.5	1.5
Invisibles	0.8						
Miscellaneous			-2.5	2.5	2.0	1.0	0.6
Current account	1.8	-3.5	-14.6	-18.9	-18.2	-17.7	-13.6
Errors and omissions	0	0	0	0	0	0	3.0
Capital account	…	…	…	…	…	17.7	10.6**
Sterling balances increase	n.a.	3.5	14.6	18.9	18.2	15.9	9.3
Other items (net)	…	…	…	…	…	1.8	1.3

*August-December. ** Excludes the issue of a Treasury Bond 1955 of £ 61.2 million as part of the settlement of sterling balances accumulated during the war.
Sources: 1940-43, Portugal-Special Account-Wartime Accruals Compared with Traditional Trade, 3.10.44, T160/1274; 1944-1945, Bank of England Dossiers, Sterling Area Balance of Payments Portugal, EID3/16.

Portugal to get it.[28] In early 1942, a Comissão Reguladora do Comércio de Metais (Metal Trade Regulatory Commission) was created and vested with the monopoly in the purchase of metals, including wolfram. An official price of wolfram (65% WO_3) of 150 escudos/kilo, including a tax of 70 escudos/kilo, was set. It was understood that the "free output" of wolfram, that is the output of mines not owned by either British or German firms, would be equally shared between the two belligerents. A quota of 2,800 tons for each of them was also fixed. Portugal and Germany signed an one year agreement on

[28] Memo of a conversation between Salazar and Campbell, 4.10.41, **Dez anos**, vol. XIV, pp.492-3.

purchases of 2800 tons.[29] Germany agreed to supply goods – chemicals, railway freight cars, iron products, paper, mining equipment -- whose value would not be less than 60% of the wolfram supplies equivalent to £ 4.2 million. The balance would be settled in Swiss francs.[30]

The Allies complained about the equal sharing of the "free wolfram" as Britain had been obtaining about three quarters before the agreement.[31] Salazar was not sympathetic to the British protests as he thought that the British had been favoured as they were more likely to fulfill their quota due to the larger production of their mines. It was one of these moments when the admiration of British officials for Salazar was severely tested.[32]

After protracted negotiations a tripartite UK-US-Portugal agreement on wolfram was signed in August 1942 to cover purchases up to 4000 tons for the year beginning 1.3.42. It covered the output of British-controlled mines and 25% of the free wolfram up to 2000 tons and 50% thereafter. This was extended to mid-1943 to coincide with other bilateral agreements on trade.

A new one-year agreement with Germany on wolfram purchases was concluded in April 1943 involving some reduction in total supplies to 2100 tons of wolfram to last until the end of February 1944.[33] It covered the output of German mines and 50% of "free wolfram". The German quid pro quo supply of goods – the same included in the previous wolfram agreement plus arms and trucks – amounted to RM 31.4 million (about £3.2 million) and corresponded to 90% of the wolfram to be supplied by Portugal under the new contract and the residual involved in the previous contract. Import prices were those of 1938 with the exception of a 10% rise in steel. This caused a rather sharp exchange of recriminations between the Allies and Portugal.[34]

In the absence of statistics on wolfram stocks – especially those of the Allies as German stocks were probably negligible -- prevents a precise answer to the question of how sales were distributed between the Allies and the Axis powers. But some indication is provided

[29] Ministério dos Negócios Estrangeiros, Acordo por troca de Notas sobre volfrâmio celebrado a 24 de janeiro de 1942 entre a Alemanha e Portugal, **Dez anos**, vol. XV, pp. 13-5 and Nunes (2010), p.347.
[30] See Telo (2000) on the postwar negotiations concerning German payments to Portugal.
[31] Eden to Monteiro, 26.2.42, **Dez anos**, vol. XV, pp.29-31.
[32] It is impossible to exaggerate their admiration. In private: "So beautiful to look at…. like Maynard Keynes, he added to the mastery of his special subjects the magic of clear, persuasive language in which with rare felicity he expressed whatever he had to say or write", Eccles (1983). p.97 or "Salazar really is a wonder: so quiet, so efficient, so romantic and, I can´t help adding, so extraordinarily fond of me", David Eccles to Sybil Eccles, 20 July 1940, Eccles (1983), p.142. Or in the official correspondence: Salazar " has the welfare of his people at heart; and that if he allows them to be police-ridden is for the reason which leads the good-natured schoolmaster to use the birch", Campbell to Eden no. 74, 4.2.1941, T160/1198. Meddlicot (1952), p. 511 tempers his enthusiasm for the "benevolent despot" with a quotation of Gordon and Dangerfield (1947), p. 103 that it "always costs more to buy a man of principle".
[33] Acordo por troca de notas sobre volfrâmio celebrado a 21 de abril de 1943 entre Alemanha e Portugal, **Dez anos**, vol. XV, pp. 288-90.
[34] Monteiro to Salazar, tesl. 180 and 181, 14.5.1943, **Dez anos,** vol. XV, pp. 300-2; British aide mémoire enclosed to Monteiro to Salazar, ofício 214, 14.5.1943, **Dez anos,** vol. XV, pp. 303-5; Salazar to Monteiro, tels. 191 e 192, 15.5.1943, **Dez anos,** vol. XV, pp. 305-9; Salazar to Monteiro, tels. 197 and 198, 16.5.1943, **Dez anos,** vol. XV, pp. 310-4.

by foreign trade statistics. The official statistics on Portuguese wolfram exports indicate that the Allies were probably right in their complaints in 1941-1942 as their aggregate imports rose only 3.9% in 1941 and fell 19.4% in 1942. German imports increased almost 10-fold in 1941 and 19.6 % in 1942. It was only in 1943 that the position was reversed as exports to the Allies more than doubled while German imports fell by almost 40%.

Table 2
Portugal: Wolfram Exports, 1936-1944, tons

	United Kingdom	United States	France	Allies	Italy	Germany	Axis	Other	Total
1936	527	0	359	886	0	358	358	76	1322
1937	618	0	413	1031	19	472	491	291	1815
1938	744	0	513	1257	10	230	240	967	2466
1939	1331	84	654	2069	0	37	37	970	3078
1940	1783	768	540	3090	30	185	215	135	3443
1941	2363	848	0	3210	173	1814	1987	36	5235
1942	2589	0	0	2589	43	2169	2212	0	4801
1943	5321	0	0	5321	0	1342	1342	5	6668
1944	1987	0	0	1986	0	701	701	0	2688

Source: Telo (2000).

Towards the end of 1943 the US government adopted an increasingly tough line concerning wolfram exports to Germany seeking a total export embargo by the Portuguese authorities. The British stance, which was initially soft, hardened after the beginning of 1944 as the US authorities remained inflexible.[35] Salazar tried to resist, insisting on strict neutrality.[36] But in spite of German protests, the Anglo-American pressures mounted. [37] Churchill wrote to Salazar pressing for interruption of sales to Germany "as any German attack upon Portugal [is] now out of the question". Salazar answered with a criticism of the Anglo-Soviet alliance, mentioned that Portuguese exports made up only a quarter of German needs of wolfram and added a reminder that when the Azores agreement had been negotiated the British had insisted that Germany would not react because of the importance they attached to their imports of wolfram and sardines from Portugal.[38] The peremptory British final request for the total prohibition of wolfram exports to Portugal invoked the Anglo-Portuguese Alliance.[39] Salazar agreed to the suspension of all production of wolfram but lamented that the Allies had not agreed to a limitation of wolfram exports to Germany which allowed exports of German-owned

[35] MEW to Lisbon, tel. 2016 ARFAR, 29.12.43, T160/1276.
[36] Salazar a Palmella, tel. 23, 15.1.44, **Dez anos,** vol. XV, pp. 392-4 ; Salazar a Bianchi, tel. 42, 24.1.44, **, Dez anos,** vol. XV, pp.397-400.
[37] Aides mémoire , interviews Salazar, Huene and Eisenlohr, 2.6.44 and 6.6.44, **Dez anos,** vol. XV, pp. 518-9 and 526-9.
[38] Churchill to Salazar, 15.3.44, enclosure to aide mémoire on meeting Salazar and Campbell, 24.3.44, **Dez anos,** vol. XV, pp. 465-7; Salazar to Churchill, 28.3.44**, Dez anos**, vol. XV**,** pp. 467-70**.** An agreement on British access to airport facilities on the Azores was signed on the 17th of August 194. This was eventually extended to cover US aircraft. See, for instance, Telo (1991), chapter VII.
[39] Even the help of Brazil was enlisted: Salazar to Nobre de Mello, tel. 44, 7.5.1944, **Dez anos,** vol. XV, pp. 490-4.

mines, doubted the legitimacy of repeatedly invoking the Alliance in matters unrelated to its letter and spirit, and mentioned losses of £8-9 million to the "national economy" and of £2 million to the Portuguese Treasury.[40]

The increase of sterling balances depended not only on much increased exports but on decreased imports. Imports from Britain and, after 1941, from the United States depended on economic blockade issues. Difficulties related to the implementation of the economic blockade by the British government persisted until the end of 1942.[41] From the very start of hostilities the hawkish views of the Ministry of Economic Warfare tended to prevail upon those of the Foreign Office, diplomats in Lisbon and the Portuguese lobby in London. A sharp animosity between Hugh Dalton, the Labour minister in charge of economic warfare, and Salazar can be perceived in the perusal of relevant documents. There were interminable frictions on import quotas, commitments on restraining re-exports and pre-blockade stocks.

In early 1941 there was a Portuguese commitment on stock limitation, navicerts in the Portuguese colonies and on re-export of goods of foreign sources. The difficulties did not abate, with Portugal resisting to restrict exports of goods produced locally.[42] Towards the end of 1942 there was a temporary truce as a War Trade Agreement with Great Britain was signed in the end of 1942 to lapse in September 1943. A supply-purchase agreement was also signed by the Allies with Portugal in the end of 1942. The British were under the impression that the Portuguese were willing to accept import surcharges that would compensate for export charges imposed on tin and wolfram.[43] This agreement was extended until the end of 1943 and renewed until mid-1945.[44]

Concern about the rising cost of imports from Portugal led to an attempt by the Allies to significantly increase the prices of their exports in the beginning of 1943. The main justification was to keep the trade deficit "within limits" and as a compensation for the heavy taxation of mineral exports by the Portuguese government, especially wolfram.[45] Ammonium sulphate, copper sulphate and oil prices among other products were increased by 100%. Salazar was outraged in spite of arguments by the Allies that prices of wolfram had been increased by 782% since the beginning of the war, prices of tin by

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[40] Campbell a Salazar, Note, 29.5.44, **Dez anos, vol.** XV, pp. 512-4; Aide mémoire meeting Salazar and Campbell, 1.6.44, **Dez anos,** vol. XV, 515-8; Salazar to Campbell, Note, 5.6.44, **Dez anos**, vol. XV, pp. 524-6.

[41] See Rosas (1990), chapter 1 and Meddlicott (1952), chapter XV (ii)..

[42] See MEW, Memorandum on the application of the quota system to Portugal, 9.3.42, **Dez anos,** vol. XV, pp. 54-7.

[43] Acordo de Fornecimento e Compras entre Portugal, o Reino Unido e os EUA, 23.11.42, enclosed to Salazar to Monteiro, tel. 433, 24.11.42, **Dez anos,** vol. XV, pp. 199-209; Supply/Purchase Agreement, memo on Anglo-American pre-emption and relations between UKCC and USCC, 23.12.42, BOE: OV6-218; Campbell to Salazar, Note, 26.1.45, Goods to be supplied by US & UK 1.1.44 to 30.6.45, **Dez anos,** vol. XV, pp. 558-65.

[44] War Trade Agreement, 28.11.42, enclosed in Salazar a Monteiro, tel. 447, 2.12.42, **Dez anos,** vol. XV, pp. 212-28.

[45] MEW to Washington, tel. 6199 ARFAR, 19.11.42, BOE: OV6-217; 6 Medlicott (1959), pp. 584-and Telo (1991), vol. 1, cap. IX.

755%, prices of rosin by 318%, prices of turpentine by 257% and prices of sardines by 219%. The Allies argued also that the proposed price increases would cover only 50% of the wolfram tax but, with an eye in the Azores negotiations, ended by agreeing to lower most increases to 50%.[46]

Between 1939 and 1942 import prices rose by between 106.8% and 113.6% depending on the weights used and a further 13-23% between 1942 and 1945. This implies a fall in import volumes of the more than 40% between 1939 and 1942. In 1945 import volumes were still almost 20% below 1939. Terms of trade improved significantly until 1942 – by more than 33% using 1939 weights and almost 540% using 1942 weights – then deteriorated to levels from 2.1% to 12.4% below 1939.[47]

3. Settlement

After D-day the British started to consider the possibility of opening negotiations with Portugal in order if possible to get rid of the gold guarantee included in the 1940 payments agreement.[48] But they were aware that to do this they would have to transfer a substantial amount of gold to Portugal. Keynes would be satisfied if the gold obligation ceased to apply to new accretions. But it was recognized in London that if new balances did not carry a gold guarantee the Portuguese would spend them first and preserve the guaranteed balances.[49]

The structure of what would become the settlement of the sterling balances accumulated during the war was outlined in September 1944 by Álvaro de Sousa, the Vice Governor of the Bank of Portugal, who suggested that negotiations on the payments agreement should be opened. Sousa proposed that the 1940 agreement should continue until the end of hostilities and that after the war payment imbalances should be settled in gold. Sterling balances accumulated during the war would remain frozen for five years and after this be settled over 25-30 years. Interest rates of 1 ½ % and between 1 and 1 ¼ % were mentioned for the two periods. British documents do not mention a gold guarantee but given Sousa´s position during the negotiations which followed it is extremely unlikely that this was not raised. [50]

[46] Salazar a Campbell, nota 7, 16.01.1943, **Dez anos,** vol. XV, pp. 248-50; Lisbon to MEW, tel. 235 ARFAR, 22.2.43 BOE: OV6-220; US Legation to Ministry of Foreign Affairs, Aide Mémoire, 17.2.43, **Dez anos,** vol. XV, pp. 259-61; Anglo-American Economic Committee Lisbon, 42nd Meeting, Minutes, 18.3.43, BOE: OV6-221; Direção-Geral do Ministério dos Negócios Estrangeiros to London Embassy, enclosures to Ofício 17, 10.5.43, **Dez anos**, vol. XV, pp. 293-99.

[47] These import indices were computed using raw data from Rosas (1990), pp. 96-7. Using 1945 weights the terms of trade improved 23.6 % between 1939 and 1942 then a further 7.3 % until 1945.

[48] Pinsent to Wyatt, 30.6.44, Wyatt to Pinsent, 17.7.44, and enclosures, Treasury meeting, Minutes, T160/1275.

[49] Keynes to Waley, 7.6.44, Playfair to Waley8.6.44, T160/1275.

[50] Tel 1589, Lisbon to London, 16.9.44, FO371/1275 . It is reasonable to suppose that Souza was considering an immediate release of balances similar to the £15 million initially offered by the British. But this was also unreported in telegram 1589.

The British would have liked to merge negotiations on the settlement of outstanding balances with those concerning payments in the postwar period but this proved to be impossible. Even recognition that the Portuguese had “treated us generously by providing credit to us … when we were fighting alone” did not prevent comments such as “we are winning the war and they obviously want to be close to us. They should have faith in the pound and not seek to deprive us of gold which we need for other purposes.” [51] What was particularly feared was “whetting the appetites” of other holders of sterling balances in South America and in the Sterling Area.[52]

In late 1944 the British presented a proposal of settlement of sterling balances accumulated during the war. While they had hoped that Portugal would agree to hold sterling “for what is worth”, that is, without a “gold” clause the Portuguese resisted. Sterling balances were to be divided between two accounts. £ 15 million would be transferred to an Account A to cover capital goods purchases to be agreed upon by the two governments. The balance would be deposited into Account B to be repaid in gold from the 11th to the 46th year at the rate of 2 ¾% yearly. The balance of Account B would carry an yearly interest rate of 7/8%. If the balance of account A fell below £2.5 million the account would be replenished by a transfer of £ 2.5 million from account B. If there was balance in Account A at the time the balance of Account B was liquidated it would convertible into gold. [53]

The British suspected that Salazar was dragging with the financial negotiations with an eye in the final settlement concerning purchases of wolfram, but in late March 1945 the Portuguese reacted to the British proposal.[54] The Portuguese authorities, besides insisting on gold clause, thought that the repayment period suggested was excessively long and proposed a repayment schedule that would start in the sixth year at the rate of 5% of the initial balance, that is five plus 20 years rather than the 10 plus 36 years proposed by the British. The British proposal on the replenishment of Account A was modified so that a minimum balance of £2.5 million would be maintained by transfers of multiples of £50,000. The possibility of running a balance of payments deficit with the Sterling Area of up to 50% of the scheduled amortization payments was also mentioned but the idea was dropped.[55]

Portugal insisted for the start of repayments after 5 years in line with the provisions of the 1940 Payments Agreement but Britain stuck to 10 years offering to shorten the repayment period to twenty years. [56] Agreement was reached and was the basis for an

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[51] Ellis-Rees to Waley, 17.10.44, T160/1275. Sir David Waley put it quite bluntly. Negotiations with Portugal depended crucially on securing that “Dr Salazar´s philosophy overcomes his cupidity”, Waley to Eady, 17.11.44, T160/1275.
[52] Cobbold to Waley, 2.11.44, Waley to Eady, 17.11.44, T160/1275.
[53] Draft letter agreed with the Bank of Portugal, enclosure to Ellis-Rees to Garran, 4.1.45, FO371-49479. Keynes had been in doubt about payments in gold after only five years as proposed by Sousa, Keynes to Waley, 6.11.44, T60/1275.
[54] Salazar to Palmella, tels. 159 to 163, 25.4.45, **, Dez anos,** vol. XV, pp. 597-600.
[55] Memorandum handed to Ashley Clarke, 14.4.45, **Dez anos,** vol. XV, pp. 600-3.
[56] Memorandum, 28.6.45, enclosed in Mathias to Neves, ofício 26, 30.6.45, **Dez anos,** vol. XV, pp. 614-6; London to Lisbon, tel. 392, 7.6.45, FO371-49481; London to Lisbon, tel. 510, 16.7.45 and tel. 740, Lisbon

exchange of letters between the Bank of England and Bank of Portugal was dated 8th of August, 1945, exactly 3 months after V-E Day as stipulated in 1940. The Bank of Portugal letter was backed by a letter by Salazar addressed to the British Ambassador stating the agreement of the Portuguese government.[57] Outstanding sterling balances as of 8.8.45 amounted to £76,195,000. Of these £15 million were deposited in Account A for capital goods expenditure as already mentioned. The residual £61,195,000 was covered by a Treasury Bond issued on the 1st November 1945 with installments falling due yearly after the 9th of August 1955.

There were minor releases from Account B to Account A in 1948 and 1949 (see Table 3). The amount outstanding was revalued by 43.9% in 1949 and 16.7% in 1967 to take account of sterling devaluations. The yearly amortizations that started to be paid in 1955 and had been originally set at 5% of the original amount outstanding were also adjusted to take account of the two sterling devaluations.

The British government insisted with Portugal that the terms of their agreement should be kept secret concerned that the "gold guarantee" granted to Portugal could create difficulties in the negotiations with other holders of sterling balances, notably India. When prompted by the Portuguese to give publicity to the terms of the 1945 agreement after the British reached the Eady-Miranda agreement with Argentina of September 1946 -- which mentioned a revaluation guarantee -- the British insisted in postponing the move.[58] It was agreed that only a reference to the "gold clause" would be made and that other details would not be revealed.[59] In early 1947 the Portuguese Minister of Finance, Costa Leite, answered a question on the revaluation guarantees by the *deputado* Burstorff da Silva in the most general terms: by stating only that "the liquidation agreement allows, without loss of the gold guarantee, the utilization of such credits".[60] As late as 1951 when The subject of writing a history of the Bank of Portugal was broached with a well known Portuguese scholar it was clear that "only some clauses were known."[61]

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to London,18.7.45, FO371-49482. In the middle of the negotiations, the British asked and Portugal agreed, in a further demonstration of goodwill, that its sterling balances would not be adjusted to take into account an increase in the London gold price from 168 shillings and 6 pence to 173 shillings and 8 pence per fine ounce to put it in line with the US dollar-sterling exchange rate of 4.03 US$/£ and the price of gold in the United States. See Aide-Mémoire, 28.5.45, enclosed to Palmella to Salazar, ofício 225, 28.5.5, **Dez anos,** vol. XV, 607-8.

[57] Catto to Branco and Branco to Catto, 8.8.45, BOE: C44/202. Salazar to O´Malley, 8.8.45, Arquivo do Banco de Portugal, Acordos Comerciais e de Pagamentos-Inglaterra, Diversos 1935/1952.

[58] United Kingdom (1946), the reference to a gold guarantee for existing balances is in I.II 3. The nationalization of Argentina´s railways was the object of a further agreement in early 1947, United Kingdom (1947).. Lima Santos to Palmella, Ofício 399, 27.9.46, Palmella to Salazar, tel. 725, 14.10.46, **, Dez anos,** vol. XV, pp. 664-5.

[59] Palmella to Salazar, tels. 740 e 809, 21.10.46 and 20.11.46, **Dez anos,** vol. XV, pp. 665-8.

[60] Portugal (1947) , pp.125-6.

[61] Soares Branco to Costa Leite, 29.9.50, reporting an interview with Teixeira Ribeiro. Soares Branco summary of the agreements on sterling balances was that Portugal treated Britain with magnanimity by providing a "blank cheque" – quoting Ellis-Rees -- and Britain reciprocated by providing gold guarantees offered to no other country.

Table 3
Portuguese Sterling Account B, 1945-1972, £ million*

	Transfers to Account A	Revaluation adjustment	Amortization	Balance
August 1945				61.2
1945				61.2
1946				61.2
1947				61.2
February 1948	3.8			
1948				57.4
September 1949		25.2		
September 1949				82.6
? 1949	1.6			
1949 to 1954				81.0
1955			4.4	76.6
1956			4.4	72.2
1957			4.4	67.8
1958			4.4	63.4
1959			4.4	59.0
1960			4.4	54.6
1961			4.4	50.2
1962			4.4	45.8
1963			4.4	41.4
1964			4.4	37.0
1965			4.4	32.6
1966			4.4	28.2
1967		4.0	5.1	25.7
1968			5.1	22.6
1969			5.1	17.4
1970			5.1	12.3
1971			5.1	7.2
1972			2.0	2.0

*End of year unless otherwise stated.
Source: Aide Mémoire, Brief History of Portuguese Bond and A account, 21.3.55, BOE: C44/204; Treasury Bond 21.9.67.

In the early 1950s Britain tried to convince Portugal to accept redemption of the outstanding balances through yearly payments in sterling to be converted into European Payments Union units and to consequently forego the revaluation guarantees. But Portugal resisted and amortization payments were duly made by Britain between 1955 and 1973 as agreed in 1945.[62]

[62] Ellis-Rees, Minute on talk with Costa Leite, 12.10.50, T238-117; Soares Branco to Costa Leite,, 29.9.50 and Soares Branco to Siepmann, 9.12.50 both in Arquivo Histórico do Banco de Portugal, Acordos Comerciais e de Pagamentos –Inglaterra Diversos 1935/1952. .

In parallel with the negotiations on the settlement of sterling balances accumulated during the war, Britain and Portugal negotiated a monetary agreement which was signed in April 1946 to regulate bilateral payments after August 1945 when the old 1940 Payments agreement had lapsed.[63] Portugal pressed for a revaluation guarantee but the British did not budge as it was thought "perhaps a little rash to assume that there was any intention on our part to alter the value of sterling".[64] After a lot of tension which included a Portuguese decision to stop temporarily the purchase of sterling in what the British thought could result in the "rupture of financial relations with Portugal".[65] Agreement was reached by allowing some transfer of balances to Account A created by the 1945 agreement and limiting the accumulation of sterling (and reciprocally of escudos) to £5 s. Any excessive accumulation would be settled by gold set aside.[66]

The Monetary Agreement of 1946 was extended several times in the late 1940s with Portugal agreeing in several instances that excessive accumulation of sterling beyond £5 million could be transferred to Account A.[67] But all this had no implication on the implementation of the 1945 agreement about the release of sterling balances accumulated during the war.

4. Evaluation of the 1945 settlement and the impact of sterling balances accumulation on the Portuguese economy

The Anglo-Portuguese settlement of 8 August 1945 preceded the Anglo-American Financial Agreement signed in December 1945 in contrast with the settlement of sterling balances held by other countries So it was unaffected by American pressure for a "scaling down" of sterling balances which was a corollary of the Anglo-American agreement as Washington did not want to see its US$ 3,750 million loan to Britain "squandered" in settling the war-debt accumulation of sterling balances. In Britain, Churchill, Lord Cherwell and, to a less extent, Keynes, since rather early in the war had been hard liners in favour of a write off of sterling balances, especially in the case of Egypt and India.

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[63] Monetary Agreement between the Portuguese Government and the Government of the United Kingdom of Great Britain and Northern Ireland, enclosure to Palmella to Salazar, tel. 270, 16.4.1946, **Dez anos**, vol. XV, pp. 660-4.

[64] Ellis-Rees, memorandum on Negotiations in Portugal, 30.8.45, FO 371/49484.

[65] Palmella to Salazar, tel. 775, 5.12.1945, **Dez anos**, vol. XV, p. 621 and London to Lisbon, tel. 48 CAMER, 5.12.45, FO371/49485. Sir Alexander Cadogan classified the Portuguese decision as "typical Salazar behaviour", Garran to Cadogan and Cadogan´s annotations, 12.12.45, FO371/49485. The British spirit in the negotiations with Portugal is well reflected in Eady to Brand, 22.12;45, "I think we are going to have some lively negotiations with … some of our payment Agreement countries. Portugal has already became inquisitive about what is going to happen to the Sterling she accumulates during 1946. But as Portugal is rather small we have been rough and two days ago I got a whisper message that their nerve had cracked. This cracking of the nerve may possibly lead to judicious importation of good quality port. No Treasury man can go into any of the Clubs without somebody coming across saying – "When can we replenish our cellars?", Bullen, Pelly, Yasamee and Bennett (1987), pp. 14-5.

[66] Ramos to Salazar, tel. 54, 29.1.46 and Salazar to Ramos, tel. 51, 2.2..46, **Dez anos,** vol. XV, 629-32.

[67] "The Portuguese unlike the Belgians .. are anxious to do what they can to prevent our having to pay them any gold!", Cabinet. Balance of Payments. Overseas Negotiations Committee, ON(47) 54 , 29.10.47, T238/116.

They faced moderate opposition from the Bank of England and very strong opposition from the India Office and the Colonial Office. [68] T

In the case of Portugal, in contrast with other sterling balance holders, a solution based on the use of balances to purchase sterling-denominated British assets -- either direct investment in railways and other public utilities or public foreign debt -- was not possible.[69] The sterling-denominated foreign debt of Portugal had been much reduced by a conversion in 1940 of almost £ 20 million of the 3% 1902 sterling loan, corresponding to more than 53% of the total outstanding foreign debt, into a consolidated 4% internal loan. In 1945 a further £ 7.9 million were redeemed so that by the end of the year only £8.4 million of sterling-denominated were outstanding and not all of it interest bearing.[70] The stock of British direct investment in Portugal was also modest.

There were no alternatives to a financial settlement involving payments over time. The question to answer is whether this settlement was relatively favourable to Portugal both in absolute terms and in comparison with other significant sterling balance holders.

In contrast with most the settlements of other sterling balance accumulations the Anglo-Portuguese agreement of 1945 was necessarily over a long time span. So it is somewhat misleading to just compare nominal interest rates applying to outstanding balances and revaluation clauses. From this point of view the Portuguese was slightly better than other settlements such as the Eady-Miranda 1946 deal with Argentina as the applied rate of interest was 7/8% rather than ½% and both agreements carried a revaluation clause. But the South America settlements were negotiated with the expectation that the sterling balances would be used to purchase British assets, especially so British-owned railways, and not with any expectation that the balances would be held in the long term.

Evaluation of the 1945 settlement hinges on comparisons between the implicit rate of return of the settlement taking into account the revaluation clauses and the return that could have been obtained in alternative investments. Without a revaluation guarantee the rate of return of holding Portuguese sterling balances between 1945 and 1973 would have been of only 0.875%, that is the nominal rate of interest on Portuguese sterling balances. The internal rate of return implied in the 1945 settlement taking into account the revaluation of outstanding balances and of amortization payments in the wake of the sterling devaluations of 1949 and 1967 was of 3.2% . This was still considerably below the interest rate that reflected the long-term cost of borrowing in London. Using yearly yields on British consols and the cash flow implied in the 1945 settlement the rate of return would have been 5.1%.

But these comparisons may underestimate the extent of Portuguese losses involved in such a long-term arrangement to liquidate outstanding sterling balances. The post-war

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[68] Perhaps the most notorious defence of a scaling down of sterling balances was that of Hugh Dalton in a speech at the Mansion House on 7 April, 1947. See Abreu (1990), pp. 459-60.
[69] See Fforde (1992), chapter 3, Fodor (1983) and (1994), Balachandran (1998), chapter 15 and Abreu (1990) among others.
[70] Valério (1994), pp. 375, 406 and 408.

period was marked by a steep increase in the prices of capital goods which were the goods the Portuguese would have preferred to import. Between 1945 and 1974 the sterling prices of iron and steel increased four-fold. If the volume of capital goods which could have been bought at 1945 prices is compared to the volumes which could have been bought over the 1955-1973 period the implicit rate of return is -2.2%.

Some evaluations of the impact of the war on the Portuguese balance of payments have stressed that the Portuguese exports increased 4-fold between 1938 and 1942 and then an additional 16.8% in 1943 – in fact 3.4 fold and an additional 2.4% -- and that the export of strategic materials at inflated prices was beneficial to a relatively few profiteers and to the countries´ external financial and trade position.[71] These evaluations miss an essential element: most of the proceeds corresponding to increased exports in 1938-1945 resulted in increased Portuguese sterling balances and could not be used to increase imports. Almost 70% of the accumulated increases in exports between 1938 and 1945 were matched by increased sterling balances. As already mentioned, nominal imports in fact stagnated between 1938 and 1942 with import volumes falling by more than 40%. While nominal imports rose by more than 60% between 1942 and 1945 import volumes in 1945 were still almost 20% below the 1939 level.

The accumulation of sterling balances rose to a peak of more than 5.5% of Portugal´s GDP in 1942 and hovered between 4.5 and 5.6% of GDP between 1941 and 1944. Compared to other significant holder of sterling balances such as Argentina Portugal held about half the amount of sterling balances and its GDP was about a fifth of that of Argentina.[72]

Increased sterling balances as a proportion of increases in the means of payment in Portugal were never below 30% and rose to a peak of 56.3% in 1943 (see table 4). In almost all economies that accumulated substantial sterling balances this was accompanied by an acceleration of inflation. Portuguese inflation was similar to that in Argentina where the accumulation of sterling balances reached a peak of 50.9% of means of payment expansion in 1944.[73] Perhaps the relevant difference is that most of the war time Argentinean inflation occurred after the military coup in 1943 while in Portugal inflationary pressures erupted after 1941.

Could Portugal have done better? Evaluation should start taking only consideration the negotiation on the settlement of sterling balances, that is without taking into account other items of the Anglo-Portuguese bilateral agenda. Two polar scenarios could be considered. Either negotiators would consider that no sterling devaluation against“gold”, that is against the US dollar, would take place within the time span of repayment or the two sides would have had perfect foresight on the future tribulations of sterling. In the first case the gap between internal rates of return implicit in the original Portuguese proposal and in the first British proposal would be 1,25% against 0,875% . In the perfect foresight scenario internal rates of return would have been 4,02% and 2,61%

[71] Gordon and Dangerfield (1947), p. 215.
[72] Maddison (1995), pp. 165-8.
[73] Fodor (1983). p. 44.

(disregarding the British very long shot of trying to get rid of the devaluation clause) with final agreement converging to the intermediate value of 3,21%. The end result would appear to be a reasonable conciliation of initial proposals (see Table 5).[74]

Table 4
Sterling balances as a % of GDP and of increased means of payment, 1940-1945, in 1000 contos

	Sterling balance accumulation	Nominal GDP	Sterling balance accumulation as a % of GDP	Cost of living (1938=100)	Increase in means of payment	Sterling balance accumulation as a % the increase in means of payment
1938	0	23149	0	100	n.a.	0
1939	0	23381	0	94	366	0
1940	350	24500	1.43	99	1170	30.8
1941	1460	29068	5.02	111	3368	43.4
1942	1890	34021	5.56	135	5207	36.3
1943	1820	36267	5.02	153	3233	56.3
1944	1590	35123	4.53	157	3840	41.4
1945	510*	36439	1.40	172	3049	16.7

Source: Table 1 and Valério (2005).
*Until 8.8.1945. Obtained by residual.

Table 5
Implicit internal rates of return in Portuguese and British proposals on the settlement of sterling balances, 1944-1945

	Sousa September 1944	UK 1 End 1944	UK 2 End 1944	Portugal April 1944	Final August 1944
“Gold” clause	Yes	No	Yes	Yes	Yes
Interest rate					
Before 1st payment	1,5%	?	0,875%	0,875%	0,875%
During repayment	1-1,25%	?	0,875%	0,875%	0,875%
Grace period	5 years	?	10 years	5 years	10 years
Repayment period	25-30 years	?	36 years	20 years	20 years
Internal rate of return					
No devaluation	1,25%	0,875%	0,875%	0,875%	0,875%
Perfect foresight	4,02%	0,875%	2,61%	3,21%	3,21%

Sources: see text.

[74] It has been assumed that all alternatives involved short-term payment of £ 15 million for capital goods imports. This would reduce the costs to Portugal of holding balances earning less interest than the yeld on British consols by about 20% (£15 million out of a total of £76.2 million

What is unclear is why Sousa of the Bank of Portugal made an initial proposal involving such modest interest rates and such long repayment periods (in fact longer than the finally agreed). In spite of all his well known sympathy towards Britain it unlikely that he was acting without the full knowledge of Oliveira Salazar No one in the Portuguese government had autonomy to make openings on such a vital problem. There is more than a hint that, by being especially accommodating to London, Salazar was trying build up on the Azores agreement and assure that Portugal would not face problems in the postwar period to explain some of the more controversial aspects of its neutrality policy.

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