June 10, 1944

Governor Szymczak — Reply to Dr. Williams on

J. Burke Knapp — International Monetary Fund

I do not think that the remarks which Dr. Williams made on Tuesday with respect to the International Monetary Fund should be allowed to pass without further challenge. I felt reluctant to intervene in the meeting, partly because of my more or less indirect participation in the Fund project, and partly because I did not want to take too sharp issue with our guests in view of the obviously delicate situation created by the New York Bank's attitude toward this matter. However, I think that Dr. Williams' position was absolutely wrong-headed and that Professor Hansen's response, excellent as far as it went, did not meet all of the issues. I am therefore taking the liberty of giving you below some further reactions.

A distinction may be made between the long-term functions of the Fund and its functions in the transition period. Professor Hansen dealt almost entirely with the former, arguing that the objectives of the Fund should be stability in the domestic economy of member countries rather than rigid stabilization of the external value of member currencies. It is really unnecessary to argue the theoretical justification for this position since it is a simple fact that none of the major member countries, including ourselves, is going to be willing to sacrifice domestic stability for the sake of maintaining a rigid parity between its currency and that of other member countries. Dr. Williams was merely setting up a straw man by arguing that the Fund in order to succeed had to assure free exchange of all currencies at stable rates; we shall never see such a world in our time and even Dr. Williams indicated at one point in his discourse that he would seek international adjustments not only through changes in domestic policies but also through shifts in exchange rates and the use of exchange control. I was also much disturbed by Dr. Williams' attitude toward British comments on the Fund. Some of his criticism no doubt was justified, but I thought he gave the meeting the impression that any advantage which the British saw in the plan was *per se* ground for suspicion on our part. Nothing would be more unfortunate than to lose sight of the fact that an expanding world economy can redound to the mutual advantage of all trading nations.

One more general comment on the Fund's operations. Should we not bring ourselves to face squarely the simple fact that we cannot have an export surplus unless we give it away, acquire more foreign gold, or lend foreign countries the dollars which they will need? The first course is a manifest absurdity, except in the course of an emergency relief program or as a subsidy for political purposes. The second is beginning to be regarded with the skepticism which it deserves; the gold becomes sterile in our hands and its loss to the foreign countries--except as it comes out of new production--tends to aggravate their domestic monetary problems. The third course, as chimerical as the first if pursued in perpetuity, finds ample justification if the objective is to bridge over a phase of post-war reconstruction, long-term development of backward areas, or temporary disequilibria in international trade. The Fund is one agency through which this third course can be pursued, and it would by its nature "take up the slack" by financing that portion of our export surplus which was not covered in other ways. Now, any shortage of dollars which may develop in the Fund must arise because we are having an export surplus without making provision for it in other ways. It seems to me a positive merit of the Fund that its operations will confront us with our fundamental dilemma--i.e. that we must either finance our export surplus or forego it. If we refuse to finance it by contributing dollars to the Fund or otherwise, we cannot reasonably object to foreign countries eliminating it by exchange depreciation or the introduction of exchange control. Indeed we should welcome such measures as saving us from the folly of our ways.

The issue on which Dr. Williams' remarks remained substantially unchallenged, however, was his argument that the Fund did not have a useful role to play in the transition period and that its creation should wait upon the development of stability in the world economy. This seems to me almost tantamount to saying that we should establish a Fund only when there is no longer need for it. The transition period will admittedly be a time of severe exchange troubles, frequent and sometimes drastic adjustments in exchange rates, and liberal use of exchange control even by leading countries. Furthermore, emergency needs for credit will be developing which, if they are not met quickly, may produce great economic disorders and hardships. It is exactly in this chaotic set of circumstances that an International Monetary Fund could find its most fruitful field of activity.

In the first place, the choice is between uncontrolled and uncoordinated changes in exchange rates and in exchange regulations, and concerted action in these fields by the world community of trading nations. The International Monetary Fund provides for orderly adjustments and recognizes the common interest of all member countries in the exchange policies pursued by each of them. Dr. Williams would probably agree to this statement in principle but would argue that such coordination as was necessary could be achieved by agreement among a few "key countries". Here the issue is squarely posed as to whether collaboration should be truly international or merely among a few major countries. I believe that we are convinced on general grounds that the widest possible group should be brought together for these basic international decisions, recognizing that the leading countries, by reason of their prestige and importance in the world trading system, will in any case play a preponderant role in arriving at these decisions.

The more controversial question, perhaps, is whether, in the highly unstable situation which has been envisaged, the Fund ought to risk the granting of credits. I would strongly argue that it should do so, providing a cushion of credit to ease what might otherwise be very abrupt changes in exchange rates and in exchange regulations, and filling in the gaps in other programs set in motion to cover the emergency relief and reconstruction needs of member countries (especially the devastated areas in Europe and the Far East).

In the first place, if it is agreed that the Fund could play a useful role as an international council on the exchange policies of member countries, it must be recognized that this role will be more important if the Fund may bring to bear not only moral suasion but also the weapon of giving or withholding credit. In other words, it may be that credit is a necessary bait to induce member countries to abide by the recommendations of the Fund. It seems to me that the basic interest of the United States in the orderly adjustment of exchange policies in foreign countries is sufficient to justify our offering such bait.

Secondly, while there is general agreement that the Fund cannot and should not carry the burden of relief and reconstruction credits, I think it is a great mistake to say that the Fund is not intended to participate at all in the solution of these problems. In practice, the adoption of this point of view would bar membership in the Fund to any countries which had not fully regained their feet. Should not the Fund be regarded as an integral part of the general attack on post-war rehabilitation? The Fund would provide a limited but immediately available source of credit to member countries, thus giving an element of elasticity to the general reconstruction program and obviating the necessity of a precise adjustment of other credits to the actual needs. In fact, the Fund might be looked upon as an agency for "pre-financing" relief and reconstruction credits. There is no reason why the Fund should not be drawn upon to meet such needs if its advances are subsequently to be funded into long-term reconstruction loans negotiated in the open markets or provided by other national or international agencies such as the Export-Import Bank or the projected World Bank. The only possible objection to this concept, it seems to me, is that member countries might abuse the Fund privileges by remaining perpetually indebted to that agency. It is precisely at this point that the positive suggestions which Mr. Gardner has advanced concerning the payment of interest on the Fund's credits and the placing of some limitation on the term of these credits come into the picture. In other words, with these additional safeguards the Fund would be a useful--and indeed it seems to me an indispensable--instrument for financing international credit needs during the transition period. If the United States does not see fit to provide this financing through the Fund, it will almost certainly have to provide it through other channels if the job of rehabilitation is to be done.

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