INTERNATIONAL MONETARY AND FINANCIAL PROPOSALS

I. The Background of the Bretton Woods Conference

During the century of comparative peace and stability following the Napoleonic wars nations gradually were evolving certain principles of behavior in their monetary and trade relations that tended to draw them together into a cohesive world. From time to time peace was interrupted locally, as during the Franco-Prussian War. Occasionally, also, individual nations - under urgent necessity - deviated from accepted principles, as when the United States was on the greenback standard. But by and large these were temporary deviations from the pattern that was being established. They were not important enough to alter the general tendency toward wider acceptance and more definite establishment of the "rules of the game."

The First World War shattered this structure to bits. Victory became the objective; and monetary and trade relations were adjusted to contribute an immediate maximum to its achievement. As a result, the relative values of various monies - the dollar, the pound, the franc, the mark - after the war bore little or no relation to their relative values before the war. Nevertheless, with the return of peace there was a vain hope and expectation that the European countries would return to their pre-war gold parities which were considered "natural." As the distinguished authority, W. A. Brown, has stated: "Each country thought of itself as attached to gold rather than as attached to other countries through gold." The problem, unfortunately, was not - as it had been before the war - that of adapting one or a few currencies to an established world system; it was to reconstruct a world system.

Instead of seeking a cooperative and joint solution, each nation undertook to solve the problem for itself without adequate regard for the effects of its action on others or even - as it turned out - on itself in the long run. Initial efforts to stabilize continued for a long time: Austria stabilized in 1922; Germany in 1923; England in 1924; the United Kingdom in 1925; France in 1926; Italy in 1927; Norway in 1928; and Portugal in 1929. In terms of pre-war parities they stabilized at rates varying from 100 per cent in the case of the United Kingdom through 20 per cent for France to .007 per cent in the case of Austria and .0000000001 per cent (one-billionth of 1 per cent) for Germany.

The new rates had serious domestic and international repercussions because they did not reflect the relative values of the currencies in terms of domestic costs and prices. The best known illustrations are sterling, which was stabilized at too high a level in 1925, and the French franc, which was stabilized at too low a level in 1926. Unfortunately, such opposite errors do not cancel each other. Each produces its own adverse effect. Thus, the depressing effects - both domestic and international - of the restoration of sterling were not offset by the undervaluation of the franc. The piecemeal actions of individual nations had not restored a stable international system. They had created a fragile structure in which destructive stresses and strains were powerful from the outset.

As the effects of the currency mistakes of the 1920's became intolerable, countries - one after another - tried to "export their unemployment" by capturing for themselves a larger fraction of dwindling world markets and by shutting their own markets to foreigners. Obviously, each could not gain at the expense of others. Yet it is probably not an exaggeration to say that man seldom has exhibited as much ingenuity on any problem as was exhibited in the "beggar-my-neighbor" monetary and trade policies of the 1930's. Countries devalued their currencies competitively to gain illusory advantages in world markets. They entered bilateral arrangements with those neighbors upon whom they could exert economic pressure. They adopted multiple currency schemes to take advantage of those owners of their currency who had little bargaining power. They established import quotas. They adopted many other devices to retaliate against each other. The net result was to destroy domestic as well as world markets and to spread unemployment.

At long last countries came to recognize that such economic warfare destroys for every nation the very activities it is designed to protect. By following the narrow view that one country can progress only at the expense of others, each had in fact impaired its own national interest. Nations demonstrated that they cannot deal separately with economic problems that are international in scope.

A step toward joint action was taken in 1936 when the United States, England, and France agreed to consult each other before taking any important steps in matters of foreign exchange. Subsequently, Belgium, the Netherlands, and Switzerland subscribed to the Tripartite Agreement. The policy of consultation was extended in the bilateral exchange arrangements between the United States and other nations on the American continents. Considerable progress had been made in dealing with world currency problems through joint action when war again broke out.

Simultaneously and independently individuals and groups in different parts of the world became convinced that the eventual peace would not be permanent if it were ushered in by economic chaos such as followed the First World War. After extensive informal discussions, preliminary tentative plans - one for a stabilization fund and one for a clearing union - were published for critical comments and constructive suggestions in April 1943. The authors of the proposals, representatives of interested countries, many organizations, and public-spirited citizens discussed the proposals formally and informally. As a result of these discussions the area of agreement among representatives of many countries on principles was found to be very wide and a "Joint Statement by Experts on the Establishment of an International Monetary Fund of the United and Associated Nations" was published simultaneously in the capitals of many countries in April 1944.

Preliminary discussions culminated in an informal meeting among representatives of many nations in Atlantic City from June 15 to June 30, 1944. These discussions also included a preliminary exchange of views on a proposal, published on November 24, 1943, for the establishment of an International Bank for Reconstruction and Development.

Finally, representatives of forty-four nations met at Bretton Woods, New Hampshire, from July 1 to July 22, 1944 and drafted Articles of Agreement for the International Monetary Fund and for the International Bank for Reconstruction and Development.

The forty-four United Nations who signed the agreements at Bretton Woods are fully cognizant of the complexities and difficulties that confront us, but they are equally determined that the avoidable mistakes committed after the last war shall not be repeated. They began with the basic principle that an effective and lasting world monetary system can be established only through concerted action; it cannot be established by a succession of unrelated acts of many nations. There was unanimous agreement on essentials but no country had altogether its own way on methods and procedural details.

II. Purposes and Principles of the Fund and Bank

The Bretton Woods Agreements provide for two institutions: the International Monetary Fund and the International Bank for Reconstruction and Development. The purpose of the Fund is to promote world trade by assuring that currencies are relatively stable. The purpose of the Bank is to promote long-term loans to facilitate reconstruction and the development of industry and agriculture in economically undeveloped countries.

The Fund would be a permanent institution to promote international monetary cooperation by providing the machinery for consultation and collaboration on international monetary problems. A major objective would be "to promote exchange stability, to maintain orderly exchange arrangements among members, and to avoid competitive exchange depreciation." It would facilitate the creation and maintenance of a sound currency basis for the balanced growth of international trade by establishing and by assisting members in following rules of good conduct based on the proposition that exchange rates are properly matters of international concern.

The Articles of Agreement specify a procedure which recognizes the importance of changes in rates to the nation making the changes as well as to other nations. A change may be made only to correct a "fundamental disequilibrium" or basic disturbance, and then only on the proposal of a member and after consultation with the Fund. A member may not change its par value more than 10 per cent, cumulative, without concurrence of the Fund.

The Fund requires members as soon as possible to make their currencies freely convertible so that each can count on using its receipts from exports to any part of the world to pay for imports from any part of the world.

Those members who cannot assume this obligation at once are required to withdraw exchange restrictions, except on capital transactions, as soon as practicable and to consult with the Fund with respect to those that may be maintained after a relatively short period of years.

Finally, the Fund provides a means of making international payments to assure its members that, if they abide by the established rules, they may meet temporary deficits in their international balances without resorting either to deflationary measures that reduce real income and employment or to anti-social measures such as excessive tariffs or other import restrictions.

Each member is assigned a quota which determines the amount of foreign exchange it may purchase from the Fund with its own currency on specified terms and conditions. The quota in essence is an extra reserve to provide members "with opportunity to correct maladjustments in their balance of payments" and "to shorten the duration and lessen the degree" of such maladjustments. "The Fund is not intended to provide facilities for relief or reconstruction" or "to meet a sustained outflow of capital."

The International Bank for Reconstruction and Development is based on the propositions (1) that there will be opportunities for loans that will be clearly desirable from a general point of view even though they may involve more risk than private lenders feel warranted in accepting and (2) that, since such loans would be of general benefit, the risks should be shared by all members and not exclusively by those who extend the loans. The Bank would be empowered to make and participate in loans and to guarantee loans made by others.

III. The Positions of the American Bankers Association and of the New York State Bankers Association

Both the American Bankers Association and the New York State Bankers Association recommend adoption of the proposed plan for an International Bank for Reconstruction and Development and transfer to the Bank of certain functions of the proposed Fund.

Both associations oppose adoption of the Fund Agreement for essentially the same reasons although there are some variations in emphasis. The major points of difference between the Fund and the proposals of the associations will be discussed under two headings: (1) access to the Fund and (2) exchange rates and exchange controls.

(1) Access to the Fund. Probably the most basic difference is over access to the resources of the Fund. The Agreement provides that a member shall be entitled to purchase foreign exchange with its own currency - that is to borrow - from the Fund provided it satisfies the following specified conditions:

(a) The purpose is consistent with the purpose of the Fund;

(b) The amount does not exceed 25 per cent of the quota in any twelve-month period or 200 per cent of the quota in all;

(c) The member repurchases - that is, repays - at the end of each year a portion of its currency, depending upon its resources;

(d) It pays specified charges;

(e) The Fund has not otherwise limited the member or declared it ineligible to use the Fund because of prior abuses;

(f) The Fund has not declared scarce the foreign exchange the member wishes to purchase.

In addition, and more importantly in many cases, proponents of the Fund rely upon the good faith of the member and upon the quality of management of the Fund. In terms of amounts it is the good faith of the large countries especially that is involved. Essentially, the right of a member to the Fund is analogous to a limited line of credit contingent upon the borrower's satisfying conditions specified in advance. This assured extra reserve would provide members that abide by the "rules of the game" with added confidence to face the future. Even though they might never actually use the Fund, the fact that it would be available would, of itself, be an important constructive influence. On the purely financial side, each member agrees (a) that the Fund may dispose of its currency and (b) that it will reimburse the Fund for any exchange loss that may result. Hence the Fund is protected except against the extremely unlikely contingency of outright repudiation.

The associations feel that neither the enumerated nor the general protections are adequate. A prospective debtor should have no limited conditional right to borrow. To grant such a right to members of the Fund would lead to serious abuses and dissipation of the Fund's assets. Each loan should be for a specific constructive purpose and should be subject to such special conditions as may be enumerated at the time it is made. Abuse is feared particularly in the transition period. It is primarily because of their general view that credit will be available somewhere to meet every specific "constructive" purpose that the associations oppose acceptance of the Fund Agreement.

Fundamentally this issue hinges on one's judgment and belief as to the good faith of the participants. Secondarily, it depends on one's judgment as to whether the management of the Fund will operate in accordance with the expressed purposes or whether the management will be impotent to deny a prospective borrower who does not satisfy the specified conditions.

(2) Exchange rates and exchange controls. The Fund Agreement provides that a member may change the par value of its currency only to correct a fundamental disequilibrium and after it has consulted with the Fund. It may not change its par value by more than 10 per cent, cumulative, against objection of the Fund - which must be declared within three days if requested for an additional 10 per cent cumulative. The Agreement also provides that members may maintain and adapt exchange restrictions on current transactions during the transitional period but shall withdraw such restrictions as soon as possible. The Fund may declare a member ineligible to use the Fund if the member persists in maintaining restrictions inconsistent with the purposes of the Fund. Any member retaining restrictions after five years must satisfy the Fund that the further continuance of such restrictions is justifiable.

The question of exchange stability was the subject of considerable debate among the delegates at Bretton Woods. As the reporting delegate stated:

> There are some who attached so much importance to exchange stability that they desired to give the Fund great authority to prevent changes in exchange rates; while others started from the position that this was a matter of sovereign right and that there should be no suggestion of interference on the part of the Fund. In the end a text was developed and incorporated in the Articles of Agreement which strikes a course between these two extreme views. All were willing to accept this middle course. In the text which was developed there is preserved intact the principle that changes in exchange rates are matters of international concern.

Similarly, the provisions on the removal of exchange controls were a result of compromise.

The associations feel that the provisions admit more flexibility in rates and more controls than should be allowed. Neither indicates specifically how more stable rates or more rapid removal of controls may be achieved, except to recommend that these matters be left to the management of the Bank. It is not apparent how a mere shift of responsibility from the Fund to the Bank would accomplish the objectives, especially since it is not recommended that the positive powers of the Fund over rates and controls be transferred.

IV. Summary

The New York State Bankers Association states:

> The fact that the experts of the various nations met together, discussed their mutual problems, and agreed upon specific proposals, was a major accomplishment in itself and no doubt led to a better understanding of one another's problems.

Similarly, the American Bankers Association reports:

> The international discussions prior to and at Bretton Woods mark a step forward in mutual understanding among the United Nations in one area where cooperation is essential.

The significant fact is that at Bretton Woods the representatives of forty-four United Nations agreed on the type of concerted action that will be needed in the field of international finance. There was unanimous agreement on essentials even though each had to yield on methods and procedural details. Spokesmen for forty-four nations thus reconciled their differences and in good faith reached agreements of momentous importance.

If after the several years of public discussion that resulted in these agreements each nation were to insist upon having its own way completely, the possibility of joint action would appear remote. If each nation insisted on basic alterations of the agreements, the practical result would be chaos similar to that which followed the last World War. Certainly we would not secure any international monetary system in which each country would abide by the principles adopted.

For the United States to insist upon modifications would be to put us in a particularly vulnerable position. The reaction of other nations would be that we are determined to use our economic power to impose our will upon the rest of the world. The resulting blow to international cooperation would be as great as any refusal to lend additional funds should the dollar eventually become a scarce currency in the Fund. Whatever defects in handling the preliminaries, the fact remains that the Conference was called by the President of the United States and that forty-three nations responded in good faith and with a determination to agree on a course of action that would avert the blunders committed after the last war.

The "rules of the game" established in the Monetary Fund would enable each nation to know where it stands. They will also strengthen the hands of the leaders of weaker nations who may point to them as standards of good conduct that must be observed to retain or establish a position among their neighbors.

The Bank is designed to meet the imperative need for international loans on a broad scale; the Fund is designed to provide a sound currency basis for the balanced growth of international trade. Together they make possible a comprehensive program to raise standards of living and therefore to expand markets throughout the world.

The Bretton Woods Agreements represent a significant step forward in international relationships. They constitute an attempt to solve difficult problems in a way that differs greatly from the clumsy and unsuccessful approach followed at the end of the last World War. The Agreements deserve thoughtful consideration by all responsible groups of the forty-four nations. Doubts arising from the novelty of the proposals should in no way deter us from giving sympathetic and open-minded legislative treatment.

Benjamin Franklin, when he was assailed by doubts concerning the Constitution itself, pointed the way to resolve such doubts in these words:

> Mr. President, I conceive that there are several parts of this Constitution which I do not at present approve, but I am not sure that I shall never approve them. For having lived long, I have experienced many instances of being obliged by better information, or fuller consideration, to change opinions even on important subjects, which I once thought right, but found to be otherwise. * * * In these sentiments, Sir, I agree to this Constitution with all its faults, if they are such.
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> I doubt too whether any other convention we can obtain may be able to make a better Constitution. For when you assemble a number of men to have the advantage of their joint wisdom, you inevitably assemble with those men all their prejudices, their passions, their errors of opinion, their local interests and their selfish views. From such an assembly can a perfect production be expected?
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> It therefore astonishes me, Sir, to find this system approaching so near to perfection as it does; and I think it will astonish our enemies, who are waiting with confidence to hear * * * that our States are on the point of separation only to meet hereafter for the purpose of cutting one another's throats. Thus, I consent, Sir, to this Constitution because I expect no better, and because I am not sure that it is not the best. The opinions I have had of its errors are sacrificed to the public good.

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KRB