HEARINGS ON BRETTON WOODS ENABLING LEGISLATION
BEFORE HOUSE BANKING AND CURRENCY COMMITTEE
May 5, 1945 -- 10:30 A.M.
(Twenty-third day of hearings)

Mr. Roy W. McDonald, professor of law on leave from Southern Methodist University and one-time chief of the Economic Intelligence Division of the Foreign Economic Administration, appeared on invitation from Rep. Smith (R. Ohio) in opposition to the Bretton Woods Agreements as presently constituted. In a prepared statement, Mr. McDonald advocated that the International Bank be accepted and its powers increased, but that the Fund be postponed. He argued that the Bank, with minor amendments, could perform every sound function now assigned to the Fund, including collection of statistics, provision of facilities for consultation among central bankers, examination of the causes of disequilibrium and recommendations for their removal, etc. There was, however, an unsound function now assigned to the Fund. The lending authority which present proposals gave to it was almost certain to make the Fund an instrumentality of long-term credits. This would result from the fact that currency could be borrowed from the Fund without reference to the credit needs or the credit worthiness of the borrower. No definite maturity dates would be set for repayment of such loans and the interest rates to be charged were not high enough to stimulate repayment. He believed, furthermore, that the post-war situation would be such that repayment of any loans would be extremely difficult for many years. He did not think that the balance of payments of the United States within the next ten, or possibly twenty, years would permit liquidation of any foreign debts which might be contracted to this country. He opposed the Fund, finally, because he believed it would not produce exchange stabilization or lead to removal of exchange restrictions. Important enemy and neutral countries would not be included in the original membership of the Fund and would not be bound by its regulations. The Fund itself permitted changes in exchange rates with considerable freedom. The witness quoted Mr. E. E. Brown to the effect that the Fund would not refuse its consent if any first class power insisted on changing the gold value of its currency. He referred also to a speech in which Governor Szymczak suggested that a "fundamental disequilibrium" would be deemed to exist if production costs in e.g., France, were to rise above those of the United Kingdom to such an extent that the latter were able to usurp a French market. The witness argued that in such an hypothetical case, the English would argue that French devaluation created a fundamental disequilibrium for England and would in turn demand that the pound be devalued. This, he declared, looked to him like competitive depreciation. As for exchange restrictions, these would be strengthened and perpetuated under the authorization granted by the Fund for retention of such controls during the transition period, for retention or establishment of control of capital movements, and for exchange control in connection with the scarce currency provisions. Mr. McDonald estimated that the total cost to the United States might reach 7 billion dollars if this country wished to maintain the Fund in operation and to avoid operation of the scarce currency provisions against its commerce.

Rep. Brown (D. Ga.) asked for the views of the witness regarding the C.E.D. proposals. Mr. McDonald stated that he agreed with the fundamental principles which the report insisted should underlie a stabilization program but questioned the efficacy of its recommendations. If the C.E.D. could reconcile the proposition that members have an automatic right to loans with the proposition that the Fund managers can refuse certain loans, its proposals might be practicable. However, if the Bank were to handle stabilization loans, the witness felt that the Fund would retain no functions which would be required in the transition period and could safely be deferred. Rep. Wolcott (R. Mich.) suggested that the weakness in the C.E.D. report was that, although it provided that the scope of the

Bank's activity be broadened, it had not provided for restricting the operations of the Fund in the manner the report suggested they should be restricted. Mr. McDonald stated that until the managers of the Fund were empowered to examine and pass upon all applications for use of the Fund's resources, the automatic extension of credit would remain a problem.

In answer to Rep. Folger (D. N.C.) Mr. McDonald stated he would not suggest that the Fund be abandoned, but rather that it be deferred until the transition period was over. Rep. Folger suggested that the third purpose of the Fund, "to promote exchange stability, to maintain orderly exchange arrangements among members and to avoid competitive exchange depreciation" referred to a problem of immediate necessity. Mr. McDonald replied that, unless the emphasis were placed entirely on the world "promote," he considered this purpose to be an immediate impossibility and believed that the Fund itself recognized that this could not be accomplished in the transition years. Rep. Buffett (R. Neb.) asked whether the Fund's provisions for currency depreciation did not furnish a first class alibi for officialdom generally to explain the deterioration of the currencies. Mr. McDonald did not care to endorse that statement but agreed depreciation could be accomplished with less criticism under the Fund program. In answer to the further question as to whether the Fund mechanism might not accelerate depreciation of national currencies, the witness agreed that depreciation of the currency of any individual country might operate to force depreciation elsewhere. Mr. Buffett expressed the fear that the operations of the Fund in regard to currency depreciation might discourage capital accumulation in all countries since potential savers would fear depreciation. Rep. Talle (R. Iowa) reiterated his concern about the possible inflationary influence of the Fund, but no pertinent discussion resulted.

Rep. Smith (R. Ohio) contended that the world had not escaped from the World War I "transition period" prior to World War II and considered that phrase to have no significance in so far as it purported to set a time limit on certain practices. Mr. McDonald pointed out that a "minimum" of five years was usually mentioned with no reference to the possible maximum. Rep. Smith stated that the Fund provisions would "legalize" currency debasement, but the witness suggested that it would be better to say the Fund would make such action "respectable" since nothing in international law governed currency practices. Rep. Smith wondered whether the Fund arrangement might not be a forerunner of rationing of all foreign trade. The witness did not believe this to be the purpose of the plan but admitted that the rationing of dollars, if adopted, would be a step in that direction. Rep. Crawford (R. Mich.) interrupted to assert his belief that the Fund Agreement would be used to facilitate more complete control of all international transactions. Rep. Smith stated that the Fund Agreement was contrary to Sections 8 and 9 of the Federal Reserve Act which gave Congress power to change the gold content of the dollar. Mr. McDonald agreed. In response to questions by Rep. Smith, the witness expressed the opinion that the Fund Agreement would force the United States to cooperate in the enforcement of foreign exchange restrictions of foreign countries even if we should consider some of these to be confiscatory. He agreed that full exchange restrictions gave the restricting government a measure by which it might control the entire economy if it wished to do so.

Board of Governors
of the Federal Reserve System
Division of Research and Statistics

May 7, 1945