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Dear Mr. Riddle:

This is in reply to your letter of May 12, 1943, in which you enclosed a copy of your memorandum entitled "British and American Plans for International Currency Stabilization". Your comparison of the two plans is generally informative and many of the points you make are well taken. There are, however, two or three questions which you raise on which I would like to comment briefly.

I want to make it clear that the Fund as provided for in the Treasury draft proposal would not compete with the existing commercial banks or interfere with the normal channels of international trade and international banking. The Fund would not engage in the banking business although it does have some powers to deal in securities and to lend and borrow currency, powers the Fund needs for purposes of cooperating with the monetary authorities of member countries.

The Fund's operations would not interfere with free exchange markets. When a member country finds it necessary to support the exchange value of its currency, it can obtain foreign exchange from the Fund which it would channel into the market in the same manner as it has in the past. In fact, the Treasury's draft proposal specifically requires member countries to abandon exchange restrictions on current transactkons. There is a reasonable hope that with an International Stabilization Fund (or some similar agency) many countries will be in a position to restore considerable freedom in the exchange markets. It is unfortunately the fact that in the absence of an international agency similar to the proposed Fund, probably no major country, with the exception of the United States and possibly one other, would be willing to abandon exchange restrictions on current transactions.

The requirement that a member country must offer to sell to the Fund any gold and foreign exchange it acquires in excess of the amount it possessed immediately after joining the Fund is for the purpose of safeguarding the Fund against the misuse of its resources by a member country. With this provision a country cannot continue to buy foreign exchange from the Fund while at the same time accumulating excessive holdings of gold and foreign

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exchange. It should be clear that no country is under any obligation to sell gold and foreign exchange to the Fund except for its local currency or for foreign exchange acceptable to it. Under the circumstances, a country of whose currency the Fund has only a moderate amount would not in fact sell to the Fund additional accumulations of gold and foreign exchange, as the Fund would not have the local currency to pay for such purchases.

There is nothing in this provision that would compel any country to interfere with existing exchange practices and existing exchange agencies. To the extent that the Fund wishes to avail itself of the offer to sell excess accumulations of foreign exchange, the member country, through its central bank, could buy the required amounts in the market and sell them to the Fund for local currency. At such a time, when a country is accumulating gold and foreign exchange, the situation in the exchange market would make it easy for the central bank to acquire from the market the foreign exchange it wishes to sell to the Fund.

The Fund is also given power to deal in securities and to make loans. Such operations would not compete with commercial banks in financing international trade or local enterprise. Nor is it contemplated that financial aid of a budgetary character would be given to governments. The purpose of the provision for buying and selling securities and making loans is solely to permit countries without adequate money markets and with rigid monetary systems to offset any expansionist or contractionist effect that their dealings with the Fund might otherwise have. It should be noted that all such dealings can be undertaken only with the approval of the member country.

You also raise the question whether international cooperation for the stabilization of currencies should be inaugurated before a measure of post-war stability and equilibrium in international trade has been established. It seems to me that if we wait for years before undertaking currency stabilization through international cooperation, we shall be resigning ourselves to a long period of general currency instability, competitive currency depreciation, and international monetary chaos. The time to act is before rather than after such unfortunate developments.

An international agency cooperating in the stabilization of currencies can prevent the breakdown of many currencies in the post-war period, and it can facilitate and hasten the attainment of the equilibrium necessary for international monetary stability. While the Fund would be able to provide resources to member countries to meet an adverse balance of payments, it would at the same time insist on appropriate measures to restore equilibrium as a condition for the use of the resources of the Fund. Such an international agency can have a tremendous influence in bringing about the adoption of policies necessary to the establishment and maintenance of international equilibrium. In this connection it should be noted that member countries undertake to give consideration to the views of the Fund on any existing or proposed monetary policy the effect of which would be to bring about a serious disequilibrium in the balance of payments of other countries.

You speak of the danger that creditor countries might find it necessary to extend credits indefinitely in order to keep the Fund operating. There are adequate safeguarding provisions limiting the sale of foreign exchange and requiring as a condition of continued use of the resources of the Fund by a member country that it adopt appropriate measures to restore balance in its international payments position. Nor is any creditor country required to provide additional resources for the Fund. It is clearly not the purpose of the Fund to continue to provide foreign exchange resources to member countries to be used to maintain indefinitely an unbalanced international payments position. The resources of the Fund are available for use only by countries that are taking measures to adjust their balance of payments positions in a manner conducive to the restoration of equilibrium without adversely affecting the general international economic situation.

One of the great advantages of the Fund is that it would give member countries time to adopt the most appropriate measures and to maintain exchange stability while these measures are taking effect. Without the Fund, many countries will certainly resort to the easy devices of exchange depreciation, exchange control, multiple exchange rates, bilateral clearing, and other discriminatory and restrictive practices so destructive to world trade. If member countries — debtor and creditor alike — will live up to their obligations, there is every hope that we can achieve through cooperative action the maintenance of that stability in exchanges that is so essential to the restoration and balanced growth of international trade.

You suggest that the objectives of international currency stabilization might be better realized by establishing a fixed dollar-sterling rate in relation to which other countries would be aided in stabilizing their currencies by means of loans and credits arranged directly with foreign countries. It seems to me that such a system setting up blocs and satellites must have unfortunate implications. Nor should we lightly assume that any country would be willing to entrust the determination of the value of its currency and the formulation of its monetary policies to another country whose economic interests may at times be in conflict with its own. There is an enormous difference between such a subordination of the national interests of one country to a more powerful country and genuine international cooperation to stabilize currencies through an international agency.

Quite apart from this factor, it is doubtful whether the proposal will succeed in terminating the discriminatory practices that will otherwise prevent the restoration of international trade. It would appear that the setting up of a dollar bloc, a sterling bloc, and a third bloc outside the dollar or sterling group, will tend to the canalizing of trade within these blocs. It is inevitable that each bloc will adopt restrictive measures designed to compel the balancing of payments with the other blocs. The full benefits of multilateral international trade can be assured only through international cooperation. Anything less will give us autarchy, multiple currencies and bilateral clearings in a new form.

Again, I wish to express my appreciation of the opportunity to see your comments on the proposals for international monetary cooperation.

Sincerely yours,

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