

PLANS FOR INTERNATIONAL CURRENCY STABILIZATION

(By R. M. Evans, Member, Board of Governors,
Federal Reserve System, Washington, D. C.)

A great deal of study has been given to a program for creating an international currency stabilization fund in the postwar period. A currency stabilization fund would be important and useful but we should not lose sight of the fact that the mechanism of such a fund cannot, by itself, bring universal prosperity. When all is said and done, it is simply a machine for doing a job, and unless the conditions in the respective countries are carefully watched and are favorable to agriculture, industry and commerce, the machinery of a fund would not work at all and the fund by itself could not change these conditions. True, recommendations might be made to countries but the countries themselves have their own legislative and administrative machinery for making these changes and they are not going to act in accordance with the desires of other countries unless they are certain such a course would be in their own best interests.

Several of these programs were discussed at a recent meeting and one of those present asked whether or not the stabilization fund would operate to deprive industry of tariff protection. Such a question indicates that some people are expecting this machinery to undertake things that are far beyond its scope. The answer, of course, to this question is that the proposal has nothing whatsoever to do with raising or lowering tariffs. Tariffs are adjusted by Congress or by trade agreements in this country.

With a view to presenting a simplified picture of the main functions performed by a fund of this kind, I am setting forth a few of the main features of such a fund and leaving the details to those who are expert in this particular field.

When the war ends, Great Britain, Germany, Russia and other countries will try to reconvert their wartime industries to the commerce of peace as rapidly as possible. They will need foodstuffs and industrial raw materials (cotton, oil, metals, etc.) as well as machinery and other things for which they will not be able to pay by exporting their own goods and services because their factories will not be equipped for peacetime production. Many of them will be short of gold with which to make payment and they may not find it feasible to arrange private credits in financial centers. Some of the most acute situations will have to be met by direct relief measures and a United Nations organization is in the making to handle this big job. In other cases which are not so severe, the problem will be to extend credit to bridge over the period until the countries concerned can pay their own way again by exporting to the rest of the world. It is to be hoped that such credits can be arranged mostly on a long-term basis, since it will take many of the devastated countries

some time to develop production to the point where they can start repayment by exporting more than they import. Such long-term credits will have to be negotiated on a specific basis with countries like the United States, which will have a surplus of goods and services, although it may be possible to work out a plan whereby the various creditor countries can coordinate their lending activities through some international institution. Finally, however, it would seem desirable to let foreign countries have a "cushion" of short-term credit with which they could operate during the transitional period. This is one of the initial purposes of the fund, and one which can be served only by having some sort of fund set up as soon as the war ends.

For example, if England wanted to buy cotton and there were no dollars available in the market because they had all been used in the purchase of other American products, she would give the fund English pounds sterling equal to the number of American dollars needed to pay for the cotton. The rate of exchange would be fixed within relatively narrow limits. The English manufacturers would weave the cotton into goods to be sold, let us say, to America for dollars and to Brazil for cruzeiros. The dollars could then be returned to the fund and the English would receive their pounds back. The United States might want to buy some coffee from Brazil so we would trade American dollars to England for Brazilian cruzeiros, which the English received from Brazil in payment for cotton goods sold by England to Brazil. We would then use the Brazilian cruzeiros to pay for the coffee. The rate of exchange in each case would be the rate set by the fund. The English would again receive their pounds back and the fund, as far as England is concerned, would be in relative balance. It is important to understand that the fund would not in any way interfere with ordinary exchange transactions in the market. It would only handle such uncleared transactions as might develop after all dealings in the market will have been effected. It will enter into the picture at the point where gold used to enter in the gold standard days. If the conditions in the world are favorable to agriculture, commerce and industry, and if people are willing to trade with each other without being too nationalistic in their viewpoint, the fund will balance over a period of years and prove to be a simple and effective device for facilitating trade.

In this country we are vitally interested in seeing that people return to their peacetime pursuits as quickly as possible after hostilities cease. World conditions will still be chaotic, and if mass unemployment, unrest and starvation were long continued, conditions would again be ripe for a revolution -- and revolutions bring dictators. If democracy is to thrive as the future type of government, it will have to provide a steadily rising standard of living. The four freedoms will have to be visible to all.

When making loans from the fund to the war-torn countries in order to permit them to purchase raw materials and equipment, short-term credit should be given -- and of course it would be necessary, not only for the safety of the fund itself but for the well-being of the borrower,

to see that the volume of such loans is in keeping with the commerce of the country involved. Long-term loans for capital investments, such as building airways and factories and developing water power, should be outside the field covered by the machinery of the fund. The effect of such loans on the future ability of the country to pay or of our country to receive payments in goods and services would have to be carefully considered. Maybe American investors will become more internationally minded as time goes on, but the point I want to emphasize is that we should not mix long-term financing with the short-time commercial operations of the fund. It would be folly to repeat the error of the '20's and loan money that could not be repaid, and yet we must take a modest risk in order to achieve an over-all good.

You may well ask the question, "How will England sell enough goods and services to pay back the amount of money she takes from the fund at the beginning?" We might just as well face the fact now that England, or any other country for that matter, cannot pay us unless the people in America are prepared to accept goods and services in return for the material and equipment we sell. This would hold equally true for all the other members of the fund. There was a time prior to the first World War when it was unnecessary to give much thought to this particular question because the United States was in debt to the countries of the old world and day by day the interest and amortization payments fell due in American dollars and were accumulated by the British, French and other peoples. These dollars were used to purchase our cotton, wheat, automobiles and other products. However, conditions have changed. British and other foreign investments in this country have been largely liquidated. We are now out of debt to foreign countries and, instead, they are heavily indebted to us.

Assuming we want to continue in the export business, there are four courses of action to follow:

First, we could accept gold in payment for the difference between what we buy and what we sell. At the present time we have more gold than we need for commercial uses and backing for our currency. More gold would be quite useless unless we were prepared to use it in purchasing goods and services from the rest of the world.

Second, we could give away our surplus commodities and services to the rest of the world, considering such a move a WPA project to create work and employment in this country. But this would be philanthropy -- not trade -- and the question would naturally be raised, "Why wouldn't it be better to use the surplus material and labor to build houses or something that would increase the standard of living for the people in this country?" Living standards can be improved in all countries, and they must be improved if trade is to flourish. Business people in America cannot trade in a worthwhile way with bankrupt people in other lands.

The third course of action would be to make long-term loans. These loans would furnish countries with money to purchase materials they could not otherwise pay for. Long-term loans would simply postpone the day of settlement to some future time when we might be willing to accept payment in goods and services.

Our fourth course of action, which is the one we must adopt if a mechanism of this kind is to become really useful, would be to purchase sufficient goods and services from abroad to pay for what we sell. Now, transactions of this kind are not quite as complicated as one might believe. Suppose England buys some cotton, wheat, pork, machinery and automobiles from this country -- it does not necessarily follow that we must purchase directly from England in order to secure payment. We might buy coffee from Brazil and rubber from the Orient, and the money Brazil and the Orient, for instance, owe to Great Britain for goods and services purchased could be used by Great Britain to pay for its purchases from us through the fund at relatively constant rates of exchange. One of the genuine aids to business would be the relative stability of exchange rates. Future plans could be made with greater safety if these exchange rates were not subject to speculative changes from time to time.

The main point to keep in mind is that if we are going to export in a business-like way, it will be necessary to import, and if we import as much as we export, a fund can furnish the machinery to make the operation efficient and economical. But if we are unprepared to accept imports in a volume equivalent to our exports, we might just as well face reality and forget the fund because no fund of this kind could operate successfully over a period of time unless we follow the fourth course of action outlined above. In order to accomplish this result, it is not necessary to import products that would create such competition as to ruin American industry. Trading in many articles and services (in such a way that American agriculture and industry would not be injured) with other countries would help to increase employment and raise our standard of living.

Foreign trade is very similar to business between individuals. If you go down town and buy a suit of clothes or some groceries from the corner store, you ordinarily use money to pay for them. You earned the money by selling your own goods or services to someone else. As long as you do that, you are all right and the economy is all right, but if you lose your job or your crops are a failure and you do not have money to pay for the things you want, someone will have to give the money to you or you will have to borrow. If the money is given to you, that closes the transaction, but if you borrow to pay for these things you will have to sell your goods, crops or services sometime in the future to pay off the loan -- and so it is between nations.

The currency stabilization fund, by itself, is merely machinery for the smooth operation of international trade. True, it has certain supervisory functions. One function is to keep exchange rates from fluctuating too widely in order to prevent the retarding of commerce. You know

how it is in your own business -- when prices fluctuate wildly, you cannot operate efficiently or economically. Stabilization of exchanges within relatively narrow limits helps to promote trade.

The basic fact we must face at this time is not so much the particular kind of stabilization fund we are going to set up but rather the all-important question of whether our nation and the other nations of the world are going to create an atmosphere and condition in which agriculture, industry and commerce can thrive. If we do this, we will have peace and prosperity for generations to come. If not, we might just as well oil our guns and keep our ammunition dry. If, after the war, the inhabitants of countries participating in the fund are enabled to have a good standard of living, then they will be in a frame of mind to retain a peaceful and democratic type of government. If, on the other hand, agriculture, industry and commerce are throttled and retarded by unwise national policies and the selfish interests of individuals and countries, these favorable conditions will not exist and an economic stabilization fund would be just one more piece of useless machinery that started out to achieve a very desirable result but could not accomplish that purpose because conditions were against it.

American agriculture and industry cannot maintain maximum production unless a reasonable percentage of their products are exported. Surpluses of farm products and surpluses of labor will hold down our national income. Just stop and think for a moment about the national income of the postwar period. We will have to service our debt. We will have to maintain a large Army and Navy. We will have to pay the expenses of expanded social services that have been created and have proved their worth. All of this can be done and we can have a far better standard of living than we have ever enjoyed if we do sufficient business to keep our American economy operating in high gear. You hear some people say, "Well, we will live within ourselves and if others want to buy our products, let them come and get them." They might more accurately say, "Let us have unemployment and a low standard of living." But no one would publicly advocate the latter, though too often we unwittingly do things that have this bad result.

I have purposely omitted consideration of the necessary and important administrative details that will have to be worked out in order to put a stabilization fund into successful operation. I believe our Government should lay down certain general guides and leave to some capable agency the working out of the plan. Congress should demand a full and complete report each year so it can alter the course as it deems best in the interests of our country.

October 1943.