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C. E. D. Statements on the Bretton Woods Agreements

Washington, June 22 -- The attached letter and statement concerning the Bretton Woods Agreements, prepared by Ralph E. Flanders and Harry Scherman, were read before the Senate Banking and Currency Committee today. Mr. Flanders is President of the Federal Reserve Bank of Boston and is Chairman of the Research Committee of the Committee for Economic Development. Mr. Scherman is President of the Book-of-the-Month Club and is a member of the C. E. D. Research Committee.

Honorable Robert F. Wagner, Chairman,
Committee on Banking and Currency,
U. S. Senate
Washington, D. C.

Dear Senator:

As Chairman of the Research Committee of the Committee for Economic Development, I appreciate this opportunity to present our views on the Bretton Woods Agreement for the hearings before this committee.

The Committee for Economic Development is composed of businessmen who are studying the important aspects of the problem of attaining and maintaining a high level of productive employment in this country. In this study we are associated with an Advisory Board of social scientists of national and international reputation, for the most part economists, and are assisted by a competent staff.

An important part of our work has been to investigate the part to be played by foreign trade in supporting a high level of productive employment in this country. Particular attention was naturally given to the Bretton Woods proposals. After months of consideration we concluded that the Bank provided for would be most useful for our national purposes, but that the Fund as originally proposed carried with it certain dangers which greatly diminished its usefulness, and in fact might become dangerous.

My associate, Mr. Harry Scherman, has told you that we feel that the amendments made in the House have in a very large measure strengthened the weak spots in the legislation, so that we now have no hesitation in urging the adoption of the amended measure.

For my part in this written testimony I wish to present to your Committee some thoughts on what seem to us to be a number of misconceptions and misapprehensions concerning the bill as it now stands.

One of the objections is arithmetically false, yet it persists. It is assumed by some that we put up more than one half the sum. Our $2.75 billion is less than a third of the $8.8 billion total, so is nowhere near one half.

Of the largest part of the remainder--for instance the Canadian dollar, the British pound, the French franc and the currencies of other mature countries--we can be assured that they will retain high value in international trade if such trade is to exist at all.

If we are wise in our other policies we will have a generally balanced trade and will not ourselves be vulnerable to raids on our currency.

A somewhat similar misapprehension is to the effect that borrowing countries are in control of the Fund's resources and lending power. Approximately 28% of the aggregate votes would be cast by representatives of this country. Aside from the extreme unlikelihood of debtor countries "ganging up" on creditor countries, there is provision for increased voting power for creditors in all voting on use of Fund's resources.

It has been asserted that we will have to police exchange markets to prevent transactions at rates below the par values of foreign currencies. This is untrue. We have no obligation for foreign currency stability beyond buying and selling gold at a fixed price.

A great merit of the agreement is that it puts an obligation on each country to prevent a depreciation of its currency in terms of the dollar. Only if such maintenance involved serious internal distress, and then only by gradual and controlled means, can a nation depreciate its currency without subjecting itself to suspension from the use of the Fund and eventual withdrawal.

Signatory countries must remove wartime currency restrictions as soon as possible and may not impose new controls without the approval of the Fund.

This whole area of agreement on exchange policy is a new and necessary approach to stable fundamentals for international trade. It gives a foundation on which businessmen and statesmen can confidently build.

In particular it is the only means which has been proposed whereby the other great factor in world-wide trade, Great Britain, can safely gear her policy into a general agreement instead of pursuing particular and unilateral interests, which would in all probability be contrary to our own.

Much else might be said on other objections, but all that have come to my attention, at least, simmer down to misapprehension.

My own greatest apprehension is that our own country may continue to be the real bad actor in world trade. Should we continue our traditional policy of trying to sell without buying, cheating ourselves and losing our shirts in the process, dollars will continue to be short and we will continue to complain about and be suspicious of "debtor countries" who are made so by our folly rather than their own.

There are signs, however, that we are losing our adolescent innocence in these matters, and that we will soon be able to hold our own in world trade. When that time comes, both we and the nations with whom we trade will profit from our new and more sensible practices, and from the benefits which both the Bank and the Fund will provide.

Ralph E. Flanders
30 Pearl Street
Boston, Massachusetts

May I identify myself as Harry Scherman, a member of the Research Committee of the Committee for Economic Development, invited by your chairman to present this written statement with regard to the Bretton Woods Agreements.

In its first statement about the Bretton Woods Agreements, published three months ago, our Research Committee set forth what it considered should be the basic principles of international monetary collaboration.

One of them was as follows: "Loans should be truly loans, currency transactions should be currency transactions, and gifts should be gifts."

If this common-sense policy is not scrupulously followed, you invite misunderstanding, bitterness, and conflict among nations. Any effort at monetary collaboration would be badly handicapped from the beginning, and its success made highly doubtful.

The bill which your Committee is considering does observe this basic principle. Indeed, it seems to be wholly inspired by that principle. Consequently, we are for it.

Not necessarily in its exact wording. Just as discussion before the House Banking and Currency Committee resulted in some extremely valuable changes in the original bill, so the discussion here may reveal that the operations of the two great instrumentalities being set up, the Fund and the Bank, may be strengthened in some minor particulars. But we regard the broad provisions of the bill as excellent, and we hope they will be approved by this Committee and will pass the Senate unchanged.

The bill follows very closely the broad recommendations made by us, and this being so, we are in a good position to testify as to what it accomplishes.

The substance of our recommendations before the House Committee was this: <u>that there should be a clarification of the functions to be performed</u>

<u>by both the Fund and the Bank beyond the possibility of misunderstanding by any member nation or any responsible individual</u>.

It may be of help to review, briefly, just how far this clarification of functions is achieved in the present bill, and what it will involve in the daily operations of these two institutions.

First, as to the Bank. The original text of the Bretton Woods Agreements could have been read to mean--and undoubtedly was taken by many people to mean--that the Bank would only make or guarantee loans for <u>specific projects</u> of reconstruction and development. But how about stabilization loans to governments, to protect monetary reserves in some transitory period of weakness? And how about the type of assistance which Dr. John Williams described as "general purpose loans,"--again straight governmental borrowing--to help restore the economic status of some countries ravaged by the war?

Both these two types of assistance would be true loans, and according to the basic principle set up should not be handled as anything but loans--not as gifts and not as currency transactions. What was to be the function of the Bank with respect to such assistance?

Our Committee discovered, in its study, that Treasury and Federal Reserve Board and State Department officials all regarded such advances as actually coming within the province of the Bank, under a "special circumstance" clause dealing with the Bank's powers. The clause was general and vague. Our Committee recommended that the power of the Bank to make all such loans be express and unmistakable.

The present bill does this. It would remove any misunderstanding that may now exist, or may later arise, about how and where stabilization loans, or general restoration loans are to be handled. They are to be handled by the Bank managers.

In fact, if one reflects on the final overall effect of the provisions of the present bill, it seems fair to conclude that every request for money coming before the two institutions that can be identified as truly a loan will go to and will be handled by the Bank managers. No advance that can be identified as truly a loan is to come within the Fund's province of management.

This clearly defined function of the Bank is to be regarded in the light of the general objective of the Bank, which--it should be understood--is altogether different from that of the Fund, as I shall show. The long-term purpose of the Bank is to bring about as quickly as possible--and then to maintain--the full and ready flow of capital from one country to another, wherever it may be needed and wherever both creditor and debtor will be benefitted by the flow. That is how so much progress, on the materialistic side, has been achieved on a worldwide scale over the past hundred and fifty years. We all know the obstructions to this flow of capital that have developed in the past quarter century. This new Bank will seek to remove these blocks that have been built up to the free flow of capital over the world. The Bank can be conceived of as building operable pipelines for the world's money; and under its careful direction money can be pumped through these pipelines, wherever it is clear that economic gain--to both creditor and debtor--can be reasonably expected.

If all advances of money that can be identified as true loans--stabilization loans, general purpose loans, specific-project loans--are to be handled by the Bank managers, the principal criticism that was made of the Monetary Fund disappears.

This main criticism was that the enormous pool of money existing in the Fund would be quickly frozen; that in the transition period the need of many distressed nations would be so great that the supply of wanted currencies--like the dollar--would be drained away and replaced with an excess of unwanted currencies; and that in the end breakdown, and some pretty bad consequences, could be expected. This apprehension has validity only if it is assumed that the Fund was designed as an agency for making loans--and particularly long-term loans. It is not; certainly it is not, under the interpretations bound to result from this bill.

We have seen what the clear-cut function of the Bank is. Is the Fund's field of action also sharply defined?

Under this bill, the central bank of a member nation can come to the Fund managers and demand the sale to it of a specific currency under its automatic quota <u>only for one purpose</u>: namely, because there is a shortage of that currency in the country, arising from a temporary unbalanced situation between the imports from and exports to the country whose currency is being sought.

Now, whether this request for a specific currency is a valid one, actually arising out of such a situation, will always be determinable by the Fund managers. That will be revealed by the current conditions of the money market in the country initiating the transaction.

Moreover, the underlying causes of the situation--if they seem likely to be more than temporary in their effect--will be recognizable to the experienced central bankers asking for the money; and if recognizable to them will be recognizable to the Fund managers, who certainly will be among the most experienced men in the world in this field.

If the situation really calls for a loan, and not a currency exchange, I myself cannot conceive the responsible individuals on both sides not recognizing that fact; with the result that the demanding nation will be sent to the Bank, if it does not go there in the first place.

Fluctuations in the balance between imports and exports in many nations will occur over short periods. They always have. In the days when the gold-standard was operating universally, these shortages of currency were quickly corrected, when they arose, by the shipment of gold, obtained usually from the monetary reserves of the country experiencing the shortage. In the years after the war, and perhaps for a long time, the monetary reserves of many nations will not permit--or at any rate cannot be relied upon--to perform this very necessary function. The Monetary Fund can fairly be described, therefore, it seems to me, as an invention called into being by the necessities of our times, and designed to perform the service that "automatic" gold shipments used to perform.

It will be a great pool of money, consisting of all currencies. Access to it by any nation must be quick, not subject to the bargaining and the delays incident to the making of conditions, as in the case of loans. But the demands will be relatively small in each case--and for short periods.

If they are anything else,--if they are suspiciously large in any case, or turn out to be extended for longer and longer periods or increased in volume, by that very fact the red flag goes up to the Fund managers. These men must be presumed to be as capable and responsible as the Bank managers, and it will certainly be within their duties to consult thoroughly with the demanders and see if a loan is not indicated as a corrective of any given situation, and not an exchange transaction with the Fund. If it is, and the Fund managers have the power to decide that it is, under this bill they can divert the demander to the Bank.

In short, the basic principle set forth above would govern--in this case, currency transactions should be currency transactions and loans should be loans. The latter should not be allowed to masquerade as the former. Under this bill, that can be wholly prevented, and with good management of the two institutions, certainly would be prevented.

It will be seen that this mechanism of the Fund--the automatic exchange of currencies within limits and under safeguards--is devised as a new means of holding the value of currencies in a stable relationship to one another--insofar as that relationship can be upset by expectable temporary imbalances of trade. Some such mechanism is obviously indispensable, if we are going to achieve "stability" of currency rates at all, since free gold shipments can no longer be relied upon to perform this function.

This mechanism must be appraised, not by itself, but as part of the whole picture; and in this appraisal--as in the case of the Bank--it seems to me one should be careful never to lose sight of the main objectives.

The main objective of the Fund is altogether different from that of the Bank. To distinguish between them--the ultimate objective of the Bank (as we saw) is to restore and maintain a full and ready flow of capital over the world. The main objective of the Fund--quite plainly, when one reflects upon it--is to put an end to economic warfare among nations carried on by monetary means.

That warfare has been going on now for a full thirty years. We all know its manifestations; the competitive devaluations, and the various kinds of obstructive controls by individual nations over both the use and the value of their money.

These uncertain and unsettled monetary conditions have now plagued the whole world for a generation; they have diminished trade; they have stifled progress; they have bred distrust and fear; they certainly had considerable to do with the causation of World War II. This economic warfare carried on by monetary means must end. Every informed person in every nation recognizes this prime need. It is idle to talk about, and hopeless to consider, establishing those orderly relationships between nations which we all mean by the word "peace," unless this first-thing-first is taken care of.

Now, while everybody will agree that this is the main objective of the Monetary Fund, it seems not to have been properly appreciated in some quarters that the mechanism we have examined--of automatic exchange of currencies, under safeguards, to protect nations when they suffer a temporary imbalance of trade--is only <u>one necessary portion</u> of a larger and well-conceived scheme of attaining the objective. It is just a part of a much bigger contract among the nations. It has taken up a good deal of the public attention, because it is a new invention and is properly subject to caution. But <u>the other parts</u> of the contract are of enormous significance, also, and have been overlooked by many persons.

What else does the Fund do besides providing this protective mechanism, to the end of establishing and maintaining stable rates of exchange between currencies?

The forty-four nations represented at Bretton Woods--if they adopt the text of the document unchanged, as the United States would do under the proposed bill--agree not to institute any new exchange controls of any character.

They agree that whatever exchange controls now exist will be progressively lightened and abandoned.

They agree that if, in the case of any member nation, repressive exchange controls persist after five years, the Fund managers--representing all the other nations--can demand that something be done about it.

They agree to measure the value of their currencies by gold.

They agree that whatever original value each one sets upon its currency, thus establishing its ratio of exchange with all other currencies, <u>has to be approved by the Fund</u>--that is, by practically all other nations.

They allow for a ten per cent devaluation from this first rate, taking proper account of the difficulties of quickly setting a fair gold value on some currencies; <u>but no change in the gold value of any currency may be made thereafter without the approval of the Fund's managers</u>.

They agree that if any further unapproved change is made, the offending nation may be barred from both the Fund's and the Bank's resources--no light penalty for any nation, large or small.

It is both sobering and exciting to reflect upon what these-- and other collaborative features of the Agreements--add up to. They mean that every one of these nations recognizes that every other nation is directly and vitally affected by what it does with regard to its own money. They go beyond that, and recognize the collective right of all other nations to have some direct say in the matter.

When one reflects upon this agreement in its entirety, it seems to mark an epoch in history. Never before have independent nations--even a few, let alone practically all--agreed to accommodate their monetary powers to those of other nations for the general peace and progress of the world. This development is of more practical importance, to my mind, than what is being accomplished at San Francisco. For it represents action toward the peaceful organization of the world; well-considered and determined action. Action, not promises, in the direction of lasting peace, is what hundreds of millions of plain men and women now want their governmental managers to provide.

Every thoughtful commentator about these two proposed international institutions agrees on one point--and the text of the Agreements also points it up--that they must not be regarded as a cureall of the world's economic malaise.

They are plainly designed as only a part of the total necessary curative treatment. Other obstructions to international commerce that are not monetary in character--such as the undue use of tariffs, the provision of subsidies, protection to cartels, and similar governmental practices--call decidedly for change, if we are to have a more orderly world. The two institutions set up by this bill can only provide the basic conditions under which these other curative measures (such as are envisaged in the Economic and Social Section of the world body being organized at San Francisco) can be attempted with some hope of success.

Our Committee pointed out in its original statement that both a sound Fund and a sound Bank are needed, in order to carry out successfully the great purposes embodied in the Bretton Woods Agreements; and that the first prerequisite of "soundness" was to have the functions of both institutions very clearly delimited and recognized by all member nations.

In the ways I have indicated, the bill your committee is considering does this job of clarifying functions, and does it well. It seems to us to assure the soundness of both the Fund and the Bank. They will be workable institutions; and it is only fair to presume that they will be wisely and not unwisely administered, in full accordance with the purposes set forth in the document.

With such administration--as we put it--"hope of successful achievement of their great purposes is not unreasonable, even in the very difficult readjustment of the world economy that must take place after the war."

Preliminary, subject to revision

Means
Taylor

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GCM
1/3/45

By: The Committee for Economic Development

REVISED DRAFT

Bretton Woods
CED Report

POLICY STATEMENT

INTERNATIONAL TRADE, FOREIGN INVESTMENT AND DOMESTIC EMPLOYMENT

I. The Opportunity and Responsibility of the U.S.A. (to be developed)

II. Analyses of the Problem (to be developed)

III. General Recommendations

A. It is recommended that the United States in the long-range interests of its citizens and those of other nations take leadership in an international program for the extension of world trade on a basis which will improve world levels of living through an increased exchange of goods and services among nations and increase world productivity through the wide dissemination of improved techniques of production.

B. Such a program should be developed along the following lines --

1. The problem of attaining and maintaining a high level of productive employment in each major country should be regarded as essentially a national problem to be handled primarily through national policies dealing with internal affairs. (Note: If the introduction does not lay a clear basis for this recommendation, it should be expanded and clarified here.)

2. The maximum expansion in the current exchange of goods and services between countries should be encouraged so long as it does not seriously interfere with the powers of individual nations to deal effectively with the problems of domestic employment.

3. The movement of capital investment between countries should be encouraged where it can serve to increase substantially the productivity of the receiving countries and provided it is not supplied in amounts whose repayment will lead to economic

difficulty in the future or supplied in ways which will lead to economic imperialism. Up to this point the export of capital can legitimately contribute to current employment within the exporting country but beyond this point it should not be relied on as a technique for increasing employment.

4. Where national units are too small for effective economic development, the advantage of contiguous regional economic groups should be recognized both as a means for reducing the barriers to trade within the group and as a method of reducing the pressures for cartelization. However, regional grouping should not be used to erect greater barriers to trade between the group and other nations or groups.
5. Ready access to raw materials, markets, and modern industrial techniques should be available to all nations on equitable terms.
6. International bodies should be created to provide reasonable stability and orderly adjustment in the relation between the currencies of different nations; to facilitate the economic movement of capital; and to develop proposals for the reduction of artificial barriers to trade. (Note: Add any other agencies suggested under "Specific Recommendations.")

C. The following advantages would arise from this program for expanding world trade:

1. Expansion of world trade would help to increase the level of living in the United States through the mutually beneficial exchange of goods and services.
2. Expansion of world trade would meet a basic need of such highly industrialized countries as England whose level of living will depend to a major extent on obtaining a large volume of imports in exchange for a large volume of exports.
3. Expansion of world trade can bring about industrialization and increased productivity in the less developed countries of Latin America, Asia and other regions both through increased exchange of goods and through internal development stimulated by imports of capital.

4. Expansion of world trade can greatly benefit particular American industries. If conditions are favorable, automobiles and other durable consumers goods and industrial equipment can be exported in large and profitable volume. Cotton and tobacco have long depended to an important extent on export markets and this need will continue at least until a solution is found for the low productivity involved in their production. Greatly expanded war industries such as the airplane, machine tool, aluminum, and magnesium industries, could find foreign postwar markets for some of their output and thereby reduce somewhat the need for workers to transfer to other activities. But it must be remembered that unless this country is willing to accept gold in exchange for its exports or make permanent investments abroad, markets must be found within the country for goods and services received in exchange for these exports, either currently or when capital investments are repaid.
5. Within the limits of economically sound foreign investment, the export of capital from the United States can be legitimately used to give a direct addition to employment and by absorbing savings may also contribute indirectly to a high level of employment. But it must always be kept in mind that unless the capital exports are given away or become a permanent foreign investment, such export of capital entails future net imports in the form of gold or goods or services of a corresponding or greater volume which may subsequently intensify the problem of employment. (Note: If the meaning of the term "export of capital" is not sufficiently clarified in the introduction, it should be defined here.)
6. The increase in trade and the industrialization of less industrialized countries can reduce population pressures both by increasing the productivity of jobs in the nations of surplus population and by increasing the opportunities in nations undergoing rapid industrial development.
7. A greatly expanded and healthy world trade can help in providing a foundation for lasting peace and a successful organization for world peace can greatly increase the benefits to be derived by the peoples of each nation from increased world trade.

D. Above all else, we believe that the war has provided an extraordinary opportunity to rebuild the basis of trade between nations and presents a challenge to the exercise of boldness and imagination in the development of future economic relationships among nations.

IV. Specific Recommendations -- A Seven Point Program

In order to bring about an expansion of world trade, we recommend the following seven point program, --

A. International Aspects of High-Level Productive Employment

We believe that the greatest single contribution which the United States can make to high levels of trade and employment throughout the world is to develop and maintain a high level of employment and production within its own borders -- the objective on which all the activities of the C.E.D. are focused. In striving for high-level productive employment, neither this nation nor any other nation should attempt to increase its level of employment at the expense of other nations by currency devaluation, by increasing trade restrictions, or by subsidies. The United States should join with other nations in reducing the danger of such practices which lead directly to competitive devaluation of currencies, retaliatory restrictions on trade and competitive subsidies.

A high level of employment and production in the United States while not essential to high-level employment in other countries, would make it easier for them to attain their goal. Prosperity in this country would mean that we would import on a large scale both raw materials and finished goods and services. This would provide foreign nations with the means to buy our exports. The large volume of exchanges would allow each country to produce those things in which it had a comparative advantage and exchange them for the goods in whose production other countries had a comparative advantage. This would not only allow all countries to gain advantage from the swapping but would allow both industrial and war material producing countries to attain a high level of employment by producing the things it is organized to produce, rather than having to reorganize its internal production, with the temporary unemployment and reduction in productivity which that would involve.

The stimulus to employment within a nation which comes from a devaluation of its currency, from an increase in its trade barriers, or from instituting a subsidy of exports makes such actions appear highly desirable to the particular nation harassed by unemployment. Such was the case when the United States sought to reduce unemployment within the country by increasing tariff barriers in 1930, by reducing the gold value of the dollar in 1934 and by subsidizing exports of wheat flour and cotton. However, the stimulating effect of such measures is likely to be short lived since it is the result of the change in currency value or trade barriers or subsidy and can be expected to disappear when trade becomes adjusted to the new condition. Furthermore, such action is almost sure to bring retaliation from other nations so that competitive devaluation of currencies and mounting trade barriers and subsidies ensue. As a result there is no important net gain in employment for any country except, perhaps, for the country which moves fastest and furthest. And with such distortions of trade, the advantages of a division of labor between countries are lost. International action to reduce this danger is discussed below in dealing with currency relationships, trade barriers, and capital movement.

The policy suggested here would not prevent changes in currency values to correct a fundamental disequilibrium between countries or the use of the trade barriers and subsidies for purposes of national security or to ease a readjustment in trade relationships. It would only prevent the use of currency changes, trade barriers, and subsidies as methods of increasing employment in one country at the expense of employment in other countries.

B. War Debts

The channels for postwar trade should be cleared by eliminating all war debts owed to the United States Government. This would require:

1. Cancellation of all foreign government debt to the United States arising from World War I and the repeal of the Johnson Act which forbids private loans to the people or governments of nations in default on such debt.

2. Cancellation of all net obligations to the United States arising under lend-lease for goods and services actually used up in the war on condition that the countries concerned enter into agreed action to promote the betterment of world wide economic relations as required in the Master Lend-Lease Agreements.

Experiences suggest that this country would have benefitted if it had cancelled the debts arising from the first World War when that war came to a close and regarded the loss as a cost of winning the war. Similarly, the sinews of war supplied under lend-lease can legitimately be regarded as a part of our contribution to victory. In both cases the supplies sent to war are paid for on the battlefield in the damage they do our enemies. To clog the channels of international trade with these indefinite obligations would be contrary to the interests of the United States.

Furthermore, we believe that any effort to use these obligations as a club to obtain special concessions such as military bases from countries unwilling to make such concessions in their own interest, would be harmful to the long-run interests of this country.

However, the nations involved should be required to meet the specific conditions contained in Article VII of the Master Lend-Lease Agreements which provides that the terms of settlement of Lend-Lease obligations "shall include provision for agreed action by the United States of America and (each other country concerned), open to participation by all other countries of like mind, directed to the expansion, by appropriate international and domestic measures, of production, employment, and the exchange and consumption of goods, which are the material foundation of the liberty and welfare of all peoples; to the elimination of all forms of descriminatory treatment in international commerce, and to the reduction of tariffs and other trade barriers; and in general, to the attainment of all the economic objectives set forth in the Joint Declaration made on August 14,1941, by the President of the United States of America and the Prime Minister of the United Kingdom."

Lend-lease goods supplied by the United States and not used up in the war, should be returned to the ownership of the United States as provided in the lend-lease agreements and should be disposed of according to the principles already outlined in the C.E.D. report on "Postwar Employment and the Liquidation of War Production."

C. Relief, Rehabilitation, and Reconstruction

In cooperation with other countries, the United States Government should contribute (adequately / generously) to the relief and rehabilitation of devastated and liberated areas and should provide credits on (reasonable / favorable) terms for the reconstruction of basic community services in devastated areas.

Relief, rehabilitation, and the preliminary steps in reconstruction are not part of the normal course of trade. They must be undertaken to put the war-torn areas on their economic feet again as rapidly as possible for the good of all nations. As such they are appropriately carried on by government and do not come under the head of the normal international movements of capital.

The giving of relief and aid in rehabilitation to save the lives and health of the war populations is a responsibility of all nations in a position to contribute.

However, relief and rehabilitation alone will not provide an adequate basis for industrial reconstruction. The basic community services operated by government must be reestablished, -- police and fire services, water systems, sewage disposal, highways, school systems, hospital facilities and power, transportation, and communication systems. The reconstruction of buildings, equipment, and other facilities for rendering these services will require a considerable outlay of capital which will help to provide services not only currently but for many years in the future. Loans to central, regional, and local governments by the United States Government in cooperation with other governments would greatly speed up this basic community reconstruction. Such loans should be provided on a more liberal basis than business considerations would allow and should be regarded as intermediate between gifts and business loans. The capital should be repaid over the period in which the community facilities are in use but interest charges should be kept to a minimum. The loans should be made with particular reference to the equipment and materials which would need to be imported in order to reestablish these services.

We believe the reconstruction of industry can better be handled through private channels supplemented by an international credit organization such as a bank for reconstruction and development to be discussed below.

D. A Solid Monetary Basis for World Trade

The United States should join with other nations in establishing order in the exchange relationship between different currencies so as to provide reasonable stability in exchange rates combined with the orderly adjustments necessary to maintain fundamental equilibrium between the values of different currencies.

We believe that orderly currency relationships are a necessary condition for any extensive development of world trade; that such orderly behavior of the exchanges is unlikely if individual nations are free to devalue their own currencies without agreement or consultation with other nations; and that an international agency should be created to provide such consultation and to facilitate both stability and orderly adjustment.

We regard the proposal for an International Monetary Fund, drafted at Bretton Woods, as a long step in the right direction. It provides for the initial setting of the values of the currencies of its members on a basis of cooperation and consultation, an essential step toward exchange stability. It provides an international reserve fund for stabilizing exchange rates between members and machinery for consultation over any change proposed by a member in the value of its currency. This should add considerably to the stability of exchange rates and greatly reduce the danger of competitive devaluation of currencies. The proposal also provides for consultations and some measure of control over the prolongation of exchange controls and the freezing of foreign funds known as blocked balances. These provisions should help to deal with one of the major problems of international finance facing the world at the end of the war. In other ways also the proposal should facilitate international monetary arrangements.

On the other hand, it is questionable whether the proposal provides adequately for the orderly adjustment of exchange rates. Some latitude in adjustment is provided to take care of the difficulties of setting the initial exchange rates in a period in which fundamental relationships are obscured by the effects of war. Further limited power to adjust is provided subject to veto of the central authority, and complete freedom is granted to a country to change the value of its currency but with the risk that it will be forced to resign from the fund. Thus, in practice, there is considerable freedom for exchange rate adjustment, either directly or as it were through the back door. But there is no indication that the fund is to operate on the principle that exchange rates should be adjusted when one-sided drains on the fund continue over a considerable period or when the fund's holdings of a member's currency build up to an excessive degree. As a result, it is doubtful if there is an adequate check on the development of unbalance within the fund and there is danger that the fund would degenerate into a device by which nations with undervalued currencies would, in effect, be forced to make continuous loans to nations with overvalued currencies.

We recommend, that, if possible, the proposal be revised to take account of this weakness. If the complexities of international cooperation do not allow such revision, we recommend the ratification of the proposal accompanied by a statement of legislative intent to the effect that the United States will regard a growing or continued drain on the fund by any particular country as prima facie evidence that the country's currency is overvalued; that it will regard a growing or continued favorable balance as prima facie evidence that a country's currency is undervalued; and that, if either became serious, and is not corrected by other action of the country involved within a reasonable period, the United States will regard a change in that country's exchange rate as in order. Such a statement of legislative intent would not be a reservation on the ratification of the agreement but would serve to focus attention on the need for orderly exchange-rate adjustment when serious unbalance within the fund developed and would put other nations on notice that the United States would feel free to withdraw from the fund if it became clear that the fund was being used primarily as a device for obtaining continuous credit rather than as a device to smooth out short-run flucutations in the balance of payments.

E. Artificial Barriers to World Trade

The United States should take the lead in a program to bring about a great reduction in the artificial barriers to trade between nations whether they take the form of tariffs, direct governmental controls over trade subsidies, or restrictive business agreements. Such a program should include, --

1. The removal of wartime controls over foreign trade at the earliest moment consistent with military necessity and the immediate economic after-effects of the war.

   In the United States, it is possible that licenses and quotas on a number of goods could be lifted immediately after V-E day. Controls over the export of certain scarce commodities may need to be retained after V-J day until national inventories are partially replenished and the stored-up demand within the nation -- particularly for consumers durable goods -- is partially filled. This last possibility would depend on how much non-war production developed between V-E and V-J day.

2. The protective tariff of the United States should be lowered (1) by the continuation of negotiations under the Reciprocal Trade Agreement Act and (2) by a major horizontal cut in all duties to be adopted by the United States regardless of whether other countries follow suit or not.

   Reciprocal trade agreements can improve and refine the existing tariff arrangements but we do not believe that a major reduction in tariffs can be brought about by this means. Yet there is need to undo the work of the Smoot-Hawley Tariff Act of 1930, which raised tariff barriers that were already excessively high, and to go much further toward a freer movement of trade. An attempt to revise this tariff downward item by item would almost certainly lead to logrolling by special interests against the national interest and result in only minor reductions. Only the bold action of a large flat reduction seems likely to succeed.

In normal peace times such a large general reduction would be likely to produce serious confusion and dislocation in industry. But if made at the end of the war, it would not add to the problems of this country in the transition from war to peace and would greatly facilitate the transition of other nations. Furthermore it would allow our transition to work toward a more satisfactory and productive pattern of American industry. We would expand greatly those industries in which American labor was most productive and in which this country had a comparative advantage. We would expand least, or possibly in a few cases contract, those industries in which American labor was less productive and in which other countries had a comparative advantage. The result would be a much more productive pattern of American industry.

We believe that a major reduction in tariffs could allow most of the trade to take place which would bring a significant net addition to American welfare and to the welfare of other nations while reciprocal trade agreements could deal with special cases.

We also recognize that a major horizontal cut in tariffs might cause hardship in special cases and necessitate some provision for administrative action to ameliorate the effects in cases of extreme hardship, perhaps through temporary subsidies to ease the adjustment to the new conditions.

It will be suggested that such a large reduction should be made only if other countries agree to do likewise. This suggestion misses two important points. First, we do not recommend the reduction for the good of other countries but for the good of the United States. It is worth making whether other countries do likewise or not. Second, the

United States is likely to be the only major country in the world in a position to make such a change <u>at the end of the war</u>. Our financial condition will be solid while that of most warring countries will need careful nurturing in order to establish a stable peace. During this initial period, many countries will need to ration their imports to those things which will contribute most to their own reconstruction. The more of their exports we take, the less they will have to control what they take in exchange and the sooner such controls can be eliminated.

International cooperation to reduce the barriers to trade will be discussed below.

3. International cartels represent one of the least understood but more pervasive barriers to international trade. We regard them as tending to monopoly and the restraint of trade. We have underway an intensive study of International Cartels and Commodity Agreements on the basis of which detailed recommendations can be made both as to cartels and as to situations in which international commodity agreements might serve a useful purpose.

4. The United States should take the lead in calling an international conference aimed at the reduction of artificial barriers to trade whether in the form of tariffs, quotas, blocked balances or other government restrictions or in the form of cartels and business agreements.

We believe it of great importance for the maintenance of the peaceful relations in the world necessary to foster high levels of production and employment that trade relations between nations be worked out without acrimony. The problems of particular countries differ and no general rules such as universal free trade are likely to apply in practice. There are problems of dumping and of exploitation which need to be considered. There are problems of the relation between freedom of trade between countries and freedom to determine the level of employment within a country. There are problems of the rate at which wartime controls can be removed without disrupting the exchanges and delaying reconstruction. There are problems of cartel control and of commodity agreements between nations. There are problems as to when subsidies are legitimately employed. All these and others should be worked out within a framework of organized international consultation.

F. The International Movement of Capital

(Note: It should be remembered that this section has not been considered in detail by the Committee.)

The United States should join with other nations in establishing order in the movement of capital between nations so as to assist the reconstruction and development of war-torn countries and to increase the productivity of all countries, particularly those which are now less industrialized. As far as possible this movement of capital should be encouraged to take the form of equities, particularly partnership equities, and long-term international loans should be kept as low as is feasible. And so far as the United States is concerned, the export of capital should not be regarded as a major source of employment nor should it be in such volume as to make repayment impracticable.

We believe that a reasonable movement of capital between countries should be encouraged and would be justified by the increased productivity which it could bring about, but that disorderly credit extension such as that which developed in the late 1920's or excessive movement of capital would be harmful both to the capital-exporting and the capital-importing nations. Above all, we do not believe that the United States should finance a large and continuous export balance through loans except possibly during the period of European reconstruction.

We regard the proposal for an International Bank for Reconstruction and Development drafted at Bretton Woods as an effective instrument to give greater orderliness in the movement of loan capital and to help in supplying the very pressing and immediate need for industrial reconstruction loans. It is not likely to lead to excessive lending and can help to remove the stigma of economic imperialism from loans financed from the United States and to diffuse the risk on such loans.

However, we believe that the bulk of the capital investment made available to foreign countries, other than that for immediate reconstruction, should take the form of equity investment, preferably partnership investment.

Equity investment eliminates the serious strain which loans frequently place on the system of exchange rates when the debt is defined in the currency of the creditor nation -- an almost necessary condition for credit extension. Furthermore, it brings immediately to bear in the foreign country the knowledge of advanced techniques, engineering experience and know-how which have developed in this country. However, complete ownership of enterprises in foreign countries has the disadvantage that it raises the issue of economic imperialism.

The danger of friction or the charge of economic imperialism can be reduced without losing the advantages of equity investment by adopting the "partnership capital" arrangement. Under this arrangement a part of the capital for an enterprise would be supplied from private sources in the foreign country and part from American private sources, while control of the enterprise is divided between the two groups. Such an arrangement fits into the pattern of international trade particularly well if the American investment is sufficient to finance the equipment and other capital goods which need to be imported by the foreign country in order to establish the new enterprise while the local investment is sufficient to finance the purchase of land, labor and materials from local sources. This type of equity investment should be particularly encouraged.

Further, we would encourage the creation of an international body, as covered in the proposal for the International Bank for Reconstruction and Development, to study the international problems involved in the industrialization of the less industrialized nations. -- What rates of industrialization should be encouraged in different countries and what would constitute over-industrialization? What magnitudes of capital would be required? What countries could most effectively supply such capital and in what form? How would such movements affect the international balance of payments? -- These would be some of the questions for study and recommendation. Both capital-supplying and capital-receiving countries should participate in these studies.

We would also encourage the creation of an international body, presumably attached to the International Bank or the Monetary Fund to study the very short-run and, on the whole, arbitrary movements of capital between nations involved in quick shifts of money holdings between countries, speculation by the citizens of one country in the security markets of another, and similar developments which involve international shifts in financial capital without any economic need for a movement of real capital. How can such financial shifts be kept to a minimum or prevented from disrupting the exchanges?

Finally, and because of the importance we attach to it, we reiterate our belief that a net export of capital should not be looked upon as a major technique for stimulating employment in the United States.

G. <u>International Transportation and Communication</u>

TO:

Mr. Lunsford

B. Leroy

CONFIDENTIAL: NOT FOR RELEASE BEFORE A.M. NEWSPAPERS TUESDAY, MARCH 20, 1945

THE

Bretton Woods Proposals

A STATEMENT ON NATIONAL POLICY BY THE

Research Committee

OF THE

COMMITTEE FOR ECONOMIC DEVELOPMENT

This statement on the Bretton Woods Proposals is part of a longer policy statement that is now in preparation dealing with International Trade, Foreign Investment, and Domestic Employment.

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OF THE

COMMITTEE FOR ECONOMIC DEVELOPMENT

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Introduction

IT IS THE POLICY of the Research Committee of C.E.D. to direct its efforts toward the solving of the larger problems of the transition in the postwar period rather than to offer conclusions on matters of merely current interest. Since, however, the Bretton Woods Agreement relates to long time policy, but at the same time comes up for early action, it has seemed wise to publish this advance section of our forthcoming Policy Statement on Foreign Trade.

The Bretton Woods Proposals cover a field difficult for many citizens to understand. We therefore give herewith some elucidation to the main point of the position taken in this report.

It is a synthesis of the present opposing views about the Bretton Woods Proposals, not a compromise between them.

This synthesis is effected by the suggestion that the proposed Bank for Reconstruction and Development be given *the express power* to extend loans to member countries to help maintain, when necessary, the established parity of the borrower's currency; and also loans designed to help in the general restoration of a member's economic status after the war.

The Bank's managers could assume this power, if they decided to exercise it, under the very broad terms of one phrase in a crucial Article: "Loans made or guaranteed by the Bank shall, *except in special circumstances,* be for the purpose of specific projects of reconstruction and development." (italics ours)

The need, in many instances, of the type of loans referred to can and may be construed as "special circumstances." But the absence here of *an express power* in the Bank to make such loans is a source of misgivings that have arisen about the wisdom of attempting to operate an International Monetary Fund, of the character created by the agreements, in the immediate postwar period.

The prime purpose of the International Monetary Fund is to enable each member country, by right of membership but within set limits, to cover *temporary short..ges* of a needed currency, arising from an adverse balance of trade between it and some other member.

Perhaps the weightiest criticisms of the International Monetary Fund have centered in the expectation that the principal demands upon this pool of currencies will arise, not from such short-lived imbalances of trade, but from the very serious distortions in production and international trade relations caused by the war.

The Monetary Fund, it is held, will inevitably be put to the necessity of having to "finance unstable conditions" in many countries for an indeterminate period; its stronger currencies will quickly be drained away and replaced by weak currencies which few firms engaged in international commerce will need or want; that is, the managers of the Fund, in spite of some safeguards, will in fact be powerless to prevent the use of this pool of money for what would be in effect stabilization, reconstruction and "general purpose" loans to war-stricken countries.

Consequently, it is held, the prime intended function of the Fund, to deal with currency transactions and to correct temporary currency imbalances, would be perverted; not through expected mismanagement, but because of the underlying economic necessities of the postwar period in many war-torn nations. This result, it is anticipated, may lead to early breakdown and future serious international monetary, economic, and political difficulties.

It is certain that many member countries after the war will need stabilization, reconstruction and general purpose loans. If such loans, as this Committee proposes, are thrown expressly *within the province of the Bank's management,* where normal credit-extending considerations could be expected to govern every transaction, the International Monetary Fund could then be constantly maintained to serve its special purpose, to deal with temporary imbalances of international trade. The Fund's managers could refer to the Bank demands that would tend to transform it, from its prime and true function, into a long-term loaning agency.

It seems to this Committee that such an extension of the Bank's powers is one to which it should be easy to gain acceptance from the present forty-four signatories of the Bretton Woods Proposals. It is not a radical change; in actuality it would be a mere clarification of a present obscure phrase.

The agreements among member nations not to depreciate their currencies by unilateral action; to remove their present exchange controls progressively; to consult and cooperate closely and constantly with one another on all monetary matters; to open up, under proper safeguards, a ready flow of capital for developmental purposes over the world—these, and other features of the Bretton Woods Proposals, will constitute momentous progress in international collaboration, *if such agreements turn out to be workable and lasting.* Both a sound Fund and a sound Bank are needed to make them workable and lasting, with the functions of each instrumentality clearly delimited and recognized by all member nations.

With the simple but significant change proposed here, the soundness of both the Fund and the Bank will be better assured, and hope of successful achievement of their great purposes is not unreasonable, even in the very difficult readjustment of the world economy that must take place in the years after the war.

Ralph Flanders
Chairman, Research Committee

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COMMITTEE FOR ECONOMIC DEVELOPMENT

ON THE

Bretton Woods Proposals

THE COMMITTEE FOR ECONOMIC DEVELOPMENT as a group of business men is deeply interested in the proposals made at Bretton Woods for the establishment of an International Monetary Fund and of an International Bank for Reconstruction and Development.

The efficient movement of international trade and capital will be facilitated by orderly relations among the various currencies of the world, and by the outlawing of the use of currencies and exchange devices for purpose of international economic warfare. Also, an orderly and adequate means of providing needed capital for world reconstruction and development will hasten the restoration and growth of production and trade with beneficial consequences for world prosperity and security.

Accordingly, in the United States high levels of productivity and of the standard of living will be more easily reached and more certainly maintained *(a) if the relation between currencies is orderly,* and *(b) if the financing of reconstruction and development is promptly and soundly arranged.*

The Research Committee, therefore, believes that it is necessary to create international machinery in which the United States would participate in order to obtain orderly international currency relations; to reduce the dangers of economic warfare; to make loans, underwritings, and guarantees in connection with reconstruction, development, and currency stabilization; and to provide arrangements under which currency and other financial problems affecting world stability and prosperity can be freely and systematically discussed.

FIVE BASIC PRINCIPLES

IN ATTAINING those objectives certain principles should be observed. First, *we want the greatest order possible in international currency relationships without infringing the essential self-interest of any country.* We hope to gain the acceptance of long-term self-interest over short-run expediency in the management of currency relationships and to harmonize, so far as possible, the interests of all. We wish to eliminate caprice, unnecessary uncertainty, and hostile actions; we do not wish to interfere with the just right of peoples to deal as may seem to them proper with their own internal problems.

Second, *in so far as possible, loans should be truly loans; currency transactions should be currency transactions; and gifts should be gifts.* Lack of clarity as between intent and method at this point will produce in the future, as it has produced in the past, misunderstanding and bitterness between countries. If a gift cannot be made as a gift, it should not mask behind the facade of a loan.

Third, *in the making of loans, underwritings, and guarantees, for reconstruction and development, the amount and kind of the loan should be geared into the amount and kind of imports needed by the borrowing country for the approved reconstruction and development projects.* Uneconomic international debt should not be created for the purposes of relief or to bring about an internal expansion which might be better produced by and within the borrowing country itself.

Fourth, *we must accept for some time as a condition of orderly currency relationships within the framework of long-term self-interest of ourselves and others, the continuance of methods of exchange control that alter what otherwise would have been the free flow of trade and investment.* Although such methods are subject to abuse, they need not be harmful in themselves. The problem is that, when they are invoked, their use should be proper and not improper; and international consultation and cooperation will help attain this end.

Fifth, *creditor countries should behave like creditors,* they should adopt measures that will make it possible for a debtor willing to pay his debts to do so. *Debtor countries should behave like debtors,* they should adopt measures that make it easier for them to observe the letter and spirit of their obligations.

The Bretton Woods Proposals

THE BRETTON WOODS PROPOSALS cover two sets of machinery, an international bank and an international currency fund. This machinery is intended to provide the means for making international loans and for short-term stabilization of currencies. We believe that both these objectives are desirable, whether they are achieved through two organizations or through one.

THE INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

WE BELIEVE *that the lending objective can be accomplished satisfactorily through the proposed International Bank for Reconstruction and Development, although we do recommend some extension of its powers. The purposes of the Bank as stated do not seem to be sufficiently broad to include loans expressly intended to serve the requirements of long-continuing stabilization.* We feel that the purposes should be so broadened.

The needed general stabilization loans which would assist in orderly monetary relations might be of two sorts. There will probably be a need for long-term loans of a type for which there is no provision at present under either the Bank or the Monetary Fund. The Bank's loans, as at present provided, are to be for specific projects of reconstruction or development; but there will probably be a number of countries that will need some more general form of loan assistance than these specific projects imply—loans designed to provide for imports of a variety of goods and services *in a general restoration of a country's powers of production and trade.* There may also be a need for short-term credits to assist in the maintenance of orderly relations in currency transactions themselves. These short-term credits may be particularly needed toward the end of the transition period, as nations proceed to relax their exchange controls and to find the equilibrium rates of exchange to which their international accounts could be balanced in a freer exchange market.

The managers of the Fund require and deserve the protection to the clarity of their operation that would come from clear authority to the Bank to make loans for stabilization purposes when they are justified.

Otherwise, there will be pressure on the managers of the Fund to permit transactions not consistent with the short-term stabilization operations of a currency fund.

THE INTERNATIONAL MONETARY FUND

THE PURPOSES of the Fund are more difficult to attain than those of the Bank. The Fund is intended primarily as an agency of long-continuing monetary management. It is intended to give all member countries access to a common fund of currencies *in order to meet the short-term fluctuations in their international position*. The basic assumption for the successful operation of such a Fund is that there should be a tendency for international transactions to equalize, apart from short-term fluctuations.

The principal criticism of the Fund is that, in the abnormal conditions of the transition from war to peace, the expectation of an even-balanced position could not be realized. If serious unbalance developed, the Fund would become lop-sided, that is, frozen with unwanted currencies. The result would be much the same as though the surplus countries had made loans to the deficit countries. In this way the Bretton Woods Proposals in their present form might lead to a frozen Fund, cause international misunderstanding, and thereby be more harmful than helpful to the cause of international monetary cooperation.

This risk of failure to work during the transition has raised the question whether the establishment of the Fund is urgent. The *urgent* need will be for specific and general credits to be granted to individual countries, rather than the need of general access to a common stabilization fund, which will become more appropriate when exchange controls are in process of removal.

But the Fund also provides for other important functions. It provides for international consultation on currency and financial matters as well as for ordinary clearing of currency balances. These functions are both useful and important.

Agreement on acceptable exchange practices, which would tend to prevent capricious change in exchange rates and to eliminate the use of currency and exchange devices for purposes of economic warfare, constitute a great advance in international cooperation. But it is true that these purposes could be served, if necessary, by the Bank, at least for the time being, leaving for a later day decision on the establishment of a separate currency Fund.

However, a significant feature that might disappear, if the consultation and clearing functions now set up in the Fund should be assigned to the Bank, *is the right of member countries to exchange their own currency for that of other countries, within limits and without the approval of the management of the Fund*.

The existence of this right is valued by every country, because it dignifies its relation to the Fund and to others, because it facilitates currency transactions, and because it avoids the necessity of a country going in debt to anybody as long as its purchase of a needed currency is within the framework of a bona fide currency transaction.

This right of access gives the Fund its short-term stabilizing power, but it also leads those who have reservations about the Fund to feel that the right might be abused, with or without intent, and that the United States would be forced to take actions to unfreeze the Fund; that the United States would be blamed by others for failure to take what would be considered adequate action to protect the Fund; and that we ourselves would misjudge the distortion of the Fund, coming from the inescapable consequences of postwar readjustments, as evidence of bad faith on the part of others.

To be sure, these dangers can be minimized if the managers of the Fund have the courage and skill to invoke at the right time the protective provisions that are written into the Articles of the Fund. But there may be proper doubt as to whether the managers would be able, in fact, to exercise these powers, unless their position is strengthened.

The solution of this difficulty lies *in giving to the Bank the clear power to make loans for long-term and short-term stabilization purposes at times when such loans are needed and appropriate.*

The managers of the Fund can then refer to the Bank those transactions for which the Fund is not intended. They can also require a country to correct any seriously unbalanced currency position through recourse to the Bank when such recourse is appropriate, rather than by taking more drastic action. Thereby the Fund can be substantially protected. We believe that the danger of abuse of the Fund would largely disappear if the purposes of the Bank were broadened to include, expressly, loans intended to serve needs for long-continuing stabilization.

We attach great weight to these considerations, particularly since the essential functions of the Fund, wherever located, require support of the Bank by powers not presently existing. We urge, therefore, that the possibility of strengthening the Bank be re-examined by the Government.

Recommendations

WE RECOMMEND the approval of the International Bank for Reconstruction and Development and also recommend that at an appropriate time, which would not delay its approval, its powers

be broadened to include the extension of general long-term or short-term loans for stabilization purposes.

After the Bank is strengthened in this way, we feel that the management of the Fund should be able to use the Fund strictly for currency transactions. Accordingly, the dangers inherent in the Fund as it now stands would be substantially reduced and we would recommend that the Fund be approved.

We are well aware that the Bretton Woods proposals do not exist in a political and diplomatic vacuum. We know that there are considerations outside the proposals proper, some of which are matters of public record, some of which may not be. These considerations must be weighed by the Administration and by Congress against the risks that are inherent in (a) approving both the Fund and the Bank as now proposed, (b) approving the Fund, and the Bank strengthened as we suggest or (c) approving the Bank alone and assigning to it the currency stabilization function.

Unless the Bank is strengthened, or unless there are weighty political or diplomatic considerations, we would recommend that certain functions of the Fund be carried on by the Bank and that the establishment of the Fund be postponed.

COMMITTEE FOR ECONOMIC DEVELOPMENT

285 MADISON AVENUE • NEW YORK 17, N. Y.

THE BOARD OF TRUSTEES

CONFIDENTIAL: NOT FOR RELEASE BEFORE A.M. NEWSPAPERS TUESDAY, MARCH 20, 1945

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Third, *in the making of loans, underwritings, and guarantees, for reconstruction and development, the amount and kind of the loan should be geared into the amount and kind of imports needed by the borrowing country for the approved reconstruction and development projects.* Uneconomic international debt should not be created for the purposes of relief or to bring about an internal expansion which might be better produced by and within the borrowing country itself.

Fourth, *we must accept for some time as a condition of orderly currency relationships within the framework of long-term self-interest of ourselves and others, the continuance of methods of exchange control that alter what otherwise would have been the free flow of trade and investment.* Although such methods are subject to abuse, they need not be harmful in themselves. The problem is that, when they are invoked, their use should be proper and not improper; and international consultation and cooperation will help attain this end.

Fifth, *creditor countries should behave like creditors,* they should adopt measures that will make it possible for a debtor willing to pay his debts to do so. *Debtor countries should behave like debtors,* they should adopt measures that make it easier for them to observe the letter and spirit of their obligations.

The Bretton Woods Proposals

THE BRETTON WOODS PROPOSALS cover two sets of machinery, an international bank and an international currency fund. This machinery is intended to provide the means for making international loans and for short-term stabilization of currencies. We believe that both these objectives are desirable, whether they are achieved through two organizations or through one.

THE INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

WE BELIEVE *that the lending objective can be accomplished satisfactorily through the proposed International Bank for Reconstruction and Development, although we do recommend some extension of its powers. The purposes of the Bank as stated do not seem to be sufficiently broad tc include loans expressly intended to serve the requirements of long-continuing stabilization.* We feel that the purposes should be so broadened.

The needed general stabilization loans which would assist in orderly monetary relations might be of two sorts. There will probably be a need for long-term loans of a type for which there is no provision at present under either the Bank or the Monetary Fund. The Bank's loans, as at present provided, are to be for specific projects of reconstruction or development; but there will probably be a number of countries that will need some more general form of loan assistance than these specific projects imply—loans designed to provide for imports of a variety of goods and services *in a general restoration of a country's powers of production and trade.* There may also be a need for short-term credits to assist in the maintenance of orderly relations in currency transactions themselves. These short-term credits may be particularly needed toward the end of the transition period, as nations proceed to relax their exchange controls and to find the equilibrium rates of exchange to which their international accounts could be balanced in a freer exchange market.

The managers of the Fund require and deserve the protection to the clarity of their operation that would come from clear authority to the Bank to make loans for stabilization purposes when they are justified.

Otherwise, there will be pressure on the managers of the Fund to permit transactions not consistent with the short-term stabilization operations of a currency fund.

THE INTERNATIONAL MONETARY FUND

THE PURPOSES of the Fund are more difficult to attain than those of the Bank. The Fund is intended primarily as an agency of long-continuing monetary management. It is intended to give all member countries access to a common fund of currencies *in order to meet the short-term fluctuations in their international position*. The basic assumption for the successful operation of such a Fund is that there should be a tendency for international transactions to equalize, apart from short-term fluctuations.

The principal criticism of the Fund is that, in the abnormal conditions of the transition from war to peace, the expectation of an even-balanced position could not be realized. If serious unbalance developed, the Fund would become lop-sided, that is, frozen with unwanted currencies. The result would be much the same as though the surplus countries had made loans to the deficit countries. In this way the Bretton Woods Proposals in their present form might lead to a frozen Fund, cause international misunderstanding, and thereby be more harmful than helpful to the cause of international monetary cooperation.

This risk of failure to work during the transition has raised the question whether the establishment of the Fund is urgent. The *urgent* need will be for specific and general credits to be granted to individual countries, rather than the need of general access to a common stabilization fund, which will become more appropriate when exchange controls are in process of removal.

But the Fund also provides for other important functions. It provides for international consultation on currency and financial matters as well as for ordinary clearing of currency balances. These functions are both useful and important.

Agreement on acceptable exchange practices, which would tend to prevent capricious change in exchange rates and to eliminate the use of currency and exchange devices for purposes of economic warfare, constitute a great advance in international cooperation. But it is true that these purposes could be served, if necessary, by the Bank, at least for the time being, leaving for a later day decision on the establishment of a separate currency Fund.

However, a significant feature that might disappear, if the consultation and clearing functions now set up in the Fund should be assigned to the Bank, *is the right of member countries to exchange their own currency for that of other countries, within limits and without the approval of the management of the Fund.*

The existence of this right is valued by every country, because it dignifies its relation to the Fund and to others, because it facilitates currency transactions, and because it avoids the necessity of a country going in debt to anybody as long as its purchase of a needed currency is within the framework of a bona fide currency transaction.

This right of access gives the Fund its short-term stabilizing power, but it also leads those who have reservations about the Fund to feel that the right might be abused, with or without intent, and that the United States would be forced to take actions to unfreeze the Fund; that the United States would be blamed by others for failure to take what would be considered adequate action to protect the Fund; and that we ourselves would misjudge the distortion of the Fund, coming from the inescapable consequences of postwar readjustments, as evidence of bad faith on the part of others.

To be sure, these dangers can be minimized if the managers of the Fund have the courage and skill to invoke at the right time the protective provisions that are written into the Articles of the Fund. But there may be proper doubt as to whether the managers would be able, in fact, to exercise these powers, unless their position is strengthened.

The solution of this difficulty lies *in giving to the Bank the clear power to make loans for long-term and short-term stabilization purposes at times when such loans are needed and appropriate.*

The managers of the Fund can then refer to the Bank those transactions for which the Fund is not intended. They can also require a country to correct any seriously unbalanced currency position through recourse to the Bank when such recourse is appropriate, rather than by taking more drastic action. Thereby the Fund can be substantially protected. We believe that the danger of abuse of the Fund would largely disappear if the purposes of the Bank were broadened to include, expressly, loans intended to serve needs for long-continuing stabilization.

We attach great weight to these considerations, particularly since the essential functions of the Fund, wherever located, require support of the Bank by powers not presently existing. We urge, therefore, that the possibility of strengthening the Bank be re-examined by the Government.

Recommendations

WE RECOMMEND the approval of the International Bank for Reconstruction and Development and also recommend that at an appropriate time, which would not delay its approval, its powers

be broadened to include the extension of general long-term or short-term loans for stabilization purposes.

After the Bank is strengthened in this way, we feel that the management of the Fund should be able to use the Fund strictly for currency transactions. Accordingly, the dangers inherent in the Fund as it now stands would be substantially reduced and we would recommend that the Fund be approved.

We are well aware that the Bretton Woods proposals do not exist in a political and diplomatic vacuum. We know that there are considerations outside the proposals proper, some of which are matters of public record, some of which may not be. These considerations must be weighed by the Administration and by Congress against the risks that are inherent in (a) approving both the Fund and the Bank as now proposed, (b) approving the Fund, and the Bank strengthened as we suggest or (c) approving the Bank alone and assigning to it the currency stabilization function.

Unless the Bank is strengthened, or unless there are weighty political or diplomatic considerations, we would recommend that certain functions of the Fund be carried on by the Bank and that the establishment of the Fund be postponed.

COMMITTEE FOR ECONOMIC DEVELOPMENT

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NEWS about postwar jobs from C.E.D.

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RELEASE FOR AM PAPERS
TUESDAY - MARCH 20

(FAHNESTOCK)

Washington, March 19 -- The Research Committee of the Committee for Economic Development (C.E.D.), in a statement issued here today on the Bretton Woods Proposals, came out in favor of the International Bank for Reconstruction and Development, but urged the Government to re-examine the possibility of strengthening the Bank in one "significant" respect before the adoption of the International Monetary Fund.

The formula suggested by this group, which has been studying the subject for some months, would enable the Congress to approve the Monetary Fund unchanged, and yet meet a weighty criticism raised against it.

The C.E.D., headed by Paul G. Hoffman, is the first important group representing general business to take a stand on the Bretton Woods Proposals.

Ralph E. Flanders, Chairman of the C.E.D. Research Committee, explained here today that the recommendations of the Committee, in his opinion, were a "synthesis of the present opposing views about the Bretton Woods proposals, not a compromise between them." He expressed the opinion that the suggested amendment should easily win acceptance from the present 44 signatories of the Bretton Woods Proposals.

The C.E.D. Research Committee amendment would give "to the Bank the clear power to make loans for long-term and short-term stabilization purposes." Without such an amendment, the Committee points out that the Fund "might be abused, with or without intent, and that the United States would be forced to take actions to unfreeze the Fund; that the United States would be blamed by others for failure to take what would be considered adequate action to protect the Fund; and that we ourselves would misjudge the distortion of the Fund, coming from the inescapable consequences of postwar readjustment, as evidence of bad faith on the part of others."

Mr. Flanders said that certain features of the Bretton Woods Proposals constituted "momentous progress in international cooperation," but only if the agreements should turn out to be workable and lasting. "With the simple but significant change proposed here," he went on, "the soundness of both the Fund and the Bank will be better assured, and hope of successful achievement of their great purposes is not unreasonable, even in the very difficult readjustment of the world economy that must take place in the years after the war."

The Committee's formal recommendations follow:

"We recommend the approval of the International Bank for Reconstruction and Development and also recommend that at an appropriate time, which would not delay its approval, its powers be broadened to include the extension of general long-term or short-term loans for stabilization purposes.

"After the Bank is strengthened in this way, we feel that the management of the Fund should be able to use the Fund strictly for currency transactions. Accordingly, the dangers inherent in the Fund as it now stands would be substantially reduced and we would recommend that the Fund be approved.

"We are well aware that the Bretton Woods proposals do not exist in a political and diplomatic vacuum. We know that there are considerations outside the proposals proper, some of which are matters of public record, some of which may not be. These considerations must be weighed by the Administration and by Congress against the risks that are inherent in (a) approving both the Fund and the Bank, (b) approving the Fund, and the Bank strengthened as we suggest or (c) approving the Bank alone and assigning to it the currency stabilization function.

"Unless the Bank is strengthened, or unless there are weighty political or diplomatic considerations, we would recommend that certain functions of the Fund be carried on by the Bank and that the establishment of the Fund be postponed."

Members of the Research Committee are: Ralph E. Flanders, Chairman, President Federal Reserve Bank, Boston, Massachusetts; Chester C. Davis, Vice Chairman, President Federal Reserve Bank, St. Louis, Missouri; William Benton, Vice Chairman, Vice President, The University of Chicago, Chicago, Illinois, Donald David, Dean, Graduate School of Business Administration, Harvard University, Cambridge, Massachusetts; John F. Fennelly, partner, Glore, Forgan and Company, Chicago, Illinois; William G. Foster, Vice President, Pressed and Welded Steel Products Company, Inc., Long Island City, New York; Paul G. Hoffman, President, Studebaker Corporation, South Bend, Indiana; Eric A. Johnston, President, Brown-Johnston Company; Ernest Kanzler, Chairman of the Board, Universal Credit Corporation, Detroit, Michigan; R. Gordon Wasson, J. P. Morgan & Company, Inc., New York, New York; Raymond Rubicam, 444 Madison Avenue, New York, New York; Beardsley Ruml, Treasurer, R. H. Macy and Company, Inc., New York, New York; Harry Scherman, President, Book-of-the-Month Club, New York, New York.

The C.E.D. is an independent, non-partisan, non-profit organization sponsored by business to stimulate planning for high level, productive employment after the war. It has more than 2200 county and community organizations throughout the country, each seeking to stimulate individual employers in industry, commerce and agriculture to plan now in order to be able to offer 7 to 10 million more jobs after the war than in the best previous peacetime year.

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