xtra copies

The Bretton Woods Plan To Prevent International Financial Chaos

By EDWARD E. BROWN
Board Chairman, First National Bank of Chicago

THE United Nations Monetary and Financial Conference, held at Bretton Woods, N. H., for three weeks in July, was attended by the representatives of 44 nations. The conference met on the invitation of the United States and was the outgrowth of a series of informal bilateral discussions, beginning almost 18 months before the conference met, between technicians of 30 different countries. The technical experts of a dozen or more of the larger and more important countries, including the United States, the United Kingdom and Russia, met at Atlantic City prior to the formal conference and discussed the matters to be considered by it. Nothing was settled at Atlantic City, but discussions there gave the principal countries concerned an understanding of each other's viewpoints and greatly facilitated the later work at Bretton Woods.

The conference produced two agreements for submission to the various governments represented, one providing for the formation of an international monetary fund and the other for an international bank for reconstruction and development. Each of the two organizations as proposed is distinct and separate from the other, and each has a different purpose although the two organizations supplement each other. The international monetary fund is designed to assist the various countries of the world in settling balances due on current accounts, to promote exchange stability, and thus to facilitate the extension of a balanced growth of international trade. The bank for reconstruction and development is designed to encourage the exportation of capital for productive purposes from countries like the U. S. which are in position to export capital to countries which need such capital either because they have been devastated by the war or because they are economically undeveloped. Both institutions represent a cooperative international effort to solve problems for the common benefit of all the nations of the world. The management of both institutions is to represent and to be elected by all the countries subscribing to them.

No participant in the conference or in the preliminary meeting of the experts could fail to be impressed by the real desire of all the United and Allied Nations to work together for the common good and in doing so to modify and compromise strongly held views and opinions. This is true of all the nations represented and not least of the two strongest nations after the United States, Russia and the United Kingdom. Both agreements as finally drafted necessarily represent compromises, as all international agreements must if the world is not to dominated by a single power. The smaller powers in many cases were represented by delegates of great ability and technical knowledge, and they made important contributions to the conference. Their points of view and special interests were always carefully considered and every effort was made by the conference to recognize them when it was possible to do so.

Currency Must Be Stable

Most of you, I am sure, recognize the fact that a country cannot create or maintain any considerable degree of internal economic activity without a currency in which its citizens have sufficient confidence to make them willing to take it in trade with each other and to make contracts running for at least short periods in terms of that currency. I am sure you also recognize that if trade is to be conducted between individuals of various countries and not through the medium of a state, or state-controlled companies, that the currencies of various countries must have at least relative stability in relation to each other.

Few of us, I think, realize how tremendous the instability of the currencies of many war-devastated countries and other countries not physically devastated, but whose economies have been disrupted by the war, will be when peace comes.

At the present time lend-lease and other devices give an artificial appearance of stability to many currencies. Once peace comes, unless something drastic is done to bring about currency stabilization, economic chaos is certain to result in many countries. Economic chaos means not only practically no international trade; it also means civil war and political unrest. Witness the recent case of Greece. Economic chaos in Europe would result in much of the continent either going communistic and tying itself up with Russia or trying some form of centralized state dictatorship of the type we are now fighting to destroy. In our own interest, not only because a good volume of foreign trade may mean the difference between reasonably full employment and depression at home but because of the greatly increased military and naval expenses to which we will be put if the rest of the world is in turmoil, it is imperative that we act to prevent postwar currency chaos from developing in the countries of the world.

The proposed international monetary fund is essentially a cooperative arrangement under which each country party to it agrees to make available to the other members an amount of its currency and gold equivalent to a given amount of American dollars, which amount is called that country's quota. In return, each country gets the right, subject to various limitations and conditions, to borrow money from the fund up to the amount of its quota for the purpose of paying for imports and balancing its international payments, but with the proviso that no country shall have the right to borrow more than 25 per cent of its quota in any one year. A country borrowing must pay interest at rates which increase progressively both with the length of time that the loan remains outstanding, and with the percentage of its quota borrowed.

One frequently heard criticism of the fund is that it is premature and that the world is not ready for it. Even with the

SPEECH OF THE MONTH
(Condensed)

Made before the Chicago Association of Commerce, January 17, 1945.

recent military setbacks, it is possible that the occupied nations of Europe may soon all be liberated and major hostilities in Europe cease. If the nations of Europe are to get on their feet and are not to fall into chaos, it is necessary that at the earliest possible date they have currencies with some degree of stability and which can be recognized and used as a basis for international trade. It is almost equally necessary that many other countries, which were neither devastated nor occupied and which are exporters of foodstuffs and raw materials, but whose economies have suffered from the war, should also have national currencies with some stability if they are to export or import. While some degree of economic reconstruction and rebuilding of destroyed facilities for production and transport will have to be done in the countries which were occupied by the enemy before any considerable exports can be expected, this reconstruction will be slowed to a snail's pace if their people lack confidence in their domestic currencies. Reconstruction and currency confidence go together. To say that one must precede the other is like saying the egg must precede the hen. To say that currency stabilization must be preceded by economic reconstruction, balanced foreign trade, and balanced budgets is to put off the possibility of all these for at least a generation.

All the nations represented at Bretton Woods realized that no currency stabilization was possible in the case of a country which was engaged in civil war, or in major hostilities in its home area, or in which any considerable and unusual segment of its population was starving. On the other hand, the need of starting up international trade in Europe, South America, Africa, Australia and the Middle East is too urgent to wait until the Japanese war is finally over.

Regulations on Fund

The fund agreement provides that in no event shall the fund engage in exchange transactions until after major hostilities in Europe have ceased and, further, contains provisions designed to keep the fund from opening up its resources to a country engaged in civil war or to a country like China still fighting in its home area, or to one which has not passed the starvation stage which may in some countries temporarily follow this war.

It is also argued that the fund is too large for stabilization purposes and will therefore encourage countries to delay the necessary steps to balance their foreign payments. However, it should be realized that the dislocations in trade caused by the war will inevitably lead to much larger fluctuations in the exports and imports of many countries than would normally exist, and that the amounts required to offset disequilibriums in the balance of payments in the first few post-war years are greater than would normally be the case. If one keeps these facts in mind, the total amount of the fund ($8,800,000,000) and the quotas given the various countries of the world, including the United States with a quota of $2,750,000,000 and the United Kingdom with a quota of $1,300,000,000, do not generally appear to be too large.

Russia, with a complete system of state trade, does not require credit for strictly stabilization purposes, and it may be admitted that Russia will probably use up her quota in the first few years of the fund's existence to pay for imported capital goods necessary for her economic reconstruction. It must also be realized that once her economy is reconstructed Russia, with her large population, with an unquestionably stable government, whether one likes it or not, and with natural resources second only to those of the United States, will be in a position to repay her borrowings from the fund without difficulty.

Fund to Control Loans

It is difficult to see how any scheme for international stabilization of currencies could work with Russia not cooperating.

The most strongly urged criticism of the fund agreement is that it gives a country the right, subject to various restrictions and conditions, to borrow from the fund up to the amount of its quota.

It is argued by many that the fund should be the sole judge of the credit worthiness of countries desiring to use its resources and should have absolute discretion in the matter of granting or refusing credit. The proponents of this view say that it is impossible to conceive a sound credit organization operating on any other basis than the normal basis between lender and borrower in which the lender is the sole judge of the credit. It should be borne in mind that the fund is dealing with sovereign governments and their central banks which must know not only what their resources in hand are, but also what borrowing facilities they can count upon. A large corporation in this country whose operations may require it to use borrowed money almost always insists on its banks giving it lines of credit, which the corporation may not use, but which its management knows are available in case of need. Many large and very solvent corporations in recent years have gone further and are paying annual fees to banks in return for getting definite rights to borrow up to certain amounts over a term of years. The necessity of central banks and treasuries knowing definitely what reserve credit they can count upon is much greater than that of a business corporation.

The fund agreement recognizes this fact, but at the same time the right to draw upon the fund is a right subject to conditions, except as to initial borrowing which cannot exceed 25 per cent of a country's quota. If the fund finds that a country is using its borrowing power in a manner contrary to the purposes of the fund, it may limit further borrowings or declare the country ineligible to use the resources of the fund. Every country desiring to borrow from the fund, including its initial borrowings, must represent that it presently needs to borrow in order to make current payments which are consistent with the provisions of the agreement. And, the fund may postpone initial exchange transactions with a member country if it believes that country's condition is such that it cannot use the fund for the purposes for which it is intended, or except in a way prejudicial to the fund and its members.

Since voting rights in the fund and control of its management are closely related to the quotas of various countries and since the United States has the largest quota I think it can reasonably be assumed that the American viewpoint will dominate the management of the fund. Furthermore, if, as is certain to be the case, the American dollar is the currency most in demand after the war the knowledge on the part of other countries that the United States can withdraw if its viewpoint is flouted by the management should practically insure recognition of our views by the fund.

Changes in Currency Value

The fund is not intended to set up a fixed gold standard and tie all the currencies of the world to gold. Few, if any, countries in the world consider such a tie-up desirable. Many, probably most countries, feel today that circumstances may arise which would make a change in the gold value of their currency imperative. But the fund does make such changes more difficult, and does ensure that they will not be undertaken lightly. In the first place, every country must consult with the fund before making a change. In the second place, it must make up any reduction in the gold value of its currency held by the fund. After initial changes aggregating, up and down, a total of not more than ten percent, the fund may object to a proposed change, and if the country over the fund's objection changes the par value of its currency, it loses its right to borrow from the fund. To be sure, it is provided that the fund shall concur in a proposed change if it is satisfied that it is necessary to correct a fundamental disequilibrium, and it shall not

object to a change because of the domestic social or political policies of a member country. It is unlikely, in view of these provisions, that in the case of any first class power the fund would refuse its consent to a change in the gold value of a currency if after discussion and argument that power insisted on its necessity. But a great power rarely changes the gold parity of its currency, in peace time at least, unless forced to do so by prior changes in the parity of the currencies of other countries which upset the relative value of its currency in international transactions.

The fund would make gold the index of the value of a currency and would maintain the use of gold for the settlement of international balances. By so doing it would exercise a strong psychological influence on all countries to maintain the gold value of their currencies. Various countries at Bretton Woods argued that the fund was too much of a gold standard plan, and most of the attacks upon it in England are based upon the fact that it will make changes in the gold value of sterling too difficult. As a compromise between rigidity and flexibility the very fact that the fund is being attacked both because it ties currencies too rigidly and too flexibly to gold indicates that it is probably as fair a compromise between two points of view as could be obtained.

In spite of the fact that the fund provides for changes in the gold value of a currency and that many such changes may be made under its terms, the fund should accomplish three very desirable results: first, end the nuisance of multiple currencies after the transition period; second, do away with competitive exchange depreciation; and, third, prevent the use of currency manipulation and depreciation for predatory political and economic purposes. Germany showed the danger to the world of allowing currency manipulation for such purposes.

Eliminate Exchange Restrictions

The fund is designed primarily to facilitate international payments on current account only, and its credit facilities are limited to this purpose. It had to be recognized that the postwar period is going to be one of great difficulty and transition and that exchange controls even for payments on current account established during the war cannot be eliminated at once. No one can say how long the transitional period will last, but it is certain to be a matter of years. The fund does provide that member countries shall take all possible measures, as soon as conditions permit, to facilitate international payments and progressively to do away with present exchange restrictions. It must be admitted that the teeth given the fund to enforce the withdrawal of restrictions on current payments now in effect are weak. But, realistically, one must remember that the maintenance of many of these restrictions for some years after peace is necessary to the economic survival of various nations, and that nations are sovereign and are naturally and properly very jealous of their rights when a question of their economic survival is at stake.

Chief Objection to Plan

The objection to the fund which has the greatest popular appeal in this country is the one that except for relatively small contributions of gold by other countries the United States is allegedly the only country which will put up currency that will be really in demand. Although the American dollar will be the currency most in demand, the currencies of other countries able to export large amounts of raw materials are also certain to be in demand. Canada, Cuba and other Latin American countries are certain to be in this category. There will be a considerable demand for sterling. The fund will have a very considerable amount of gold contributed by countries other than the United States. Many countries have large gold holdings and dollar balances which they will presumably use before drawing on the fund. The fund agreement provides that as the gold holdings or holdings of American dollars of a country increase it must repay part of its borrowings from the fund.

Bearing these facts in mind and also the fact that no country has the right to draw more than 25 percent of its quota in any one year, the dollars and gold in the fund cannot under the most unfavorable circumstances become exhausted as rapidly as the objectors to the plan fear. If the United States recognizes the fundamental truth that a creditor nation must ultimately accept payment for its exports in goods, using the word "goods" to include services, the fund should be able to work indefinitely without the dollar becoming scarce. If the United States insists on continuing to export more than it imports, dollars are bound ultimately to become scarce and other countries of the world will have to discriminate against American goods no matter how much they may desire them. We can postpone that time by accepting gold or loaning money abroad. But ultimately we shall get all the gold with which the rest of the world is willing to part, and we shall become tired of loaning money for the purpose of enabling borrowers to pay for goods which we currently export, as well as interest on the money they have already borrowed.

It is to be hoped that before the dollars in the fund have become scarce the American people will have to come to a greater maturity in their economic thinking and will radically change their present tariff policy.

While it would be highly undesirable to have the American dollar declared scarce and exchange restrictions imposed against it by other countries, it should be realized that if nothing is done the dollar is bound to become generally scarce throughout the world in short order and existing exchange discriminations against it are certain to increase.

Even though the dollar is declared scarce and remains so, our contribution to the fund would not be lost. It would be frozen, to be sure, and we would lose interest on our contribution. But, barring another general world war, we could, over a period of years, convert our claim against the currencies of most of the nations held by the fund into goods and thus get most of our money back. The fund would still continue to function and the currencies of other countries would continue to be interchangeable at the parities fixed from time to time by the fund even though not convertible into dollars. This would benefit international trade and thus our own trade. Meanwhile, by our contribution to the fund we would have made possible currency stabilization in war-devasted countries and by thus helping them restore their economics we would greatly increase the chance of political stability, without which there is no chance for peace and general multilateral trade. And without these there cannot be continuing world prosperity or prosperity in this country.

U. S. Must Aid Nations

All the critics of the international monetary fund realize that the United States must in its own interest help the rest of the world get on its feet after this war is over either by gifts or by furnishing credit and taking credit risks. No proponent of the fund believes that it is a panacea, or that alone it will be sufficient to solve the economic problems of the world. Some considerable degree of currency stabilization is generally recognized as one of the indispensable things which must be provided for a reconstructed world economy.

No other plan has been suggested which involves less risk to the American people than the fund, even assuming that we still continue indefinitely our present high tariff policy.

The other plan drawn up at Bretton Woods is that of the international bank for reconstruction and development. The argument for such an institution is based on two premises, both of which I believe to be sound. The first premise is that the export of capital by a country like the United States, which is in a position to do so, to countries which have been devastated by the war or are economically undeveloped and can pro-

fitably use such capital, is a benefit not only to the particular exporting and importing countries but also to the other trading nations of the world. The second premise is that after the experience of the 20's and 30's with foreign loans no considerable amount of money will be loaned abroad, by Americans at least, at reasonable rates of interest except under some adequate governmental guarantee. At the present time, for certain classes of loans the export-import bank does give such a guarantee.

Since, however, the export of surplus capital by a country benefits not only itself and the receiving country but also all the other trading nations of the world, it is only fair that the risk involved in such lending should be shared by all such countries and not borne entirely by the exporting country.

The proposed bank developed at Bretton Woods will have a subscribed capital of $10,000,000,000, of which the United States' subscription is $3,175,000,000. The subscriptions of other countries generally correspond to their quotas in the international monetary fund. The bank will be governed by a board of directors representing the various countries, and the voting rights of these directors closely correspond with the subscriptions to the capital stock of the countries which elect them. As in the case of the fund, this means that the United States, plus a few countries whose economic thinking is like ours, will at all times be in control.

Twenty per cent of the bank's initial capital is to be paid in, one-tenth in gold or United States dollars and the balance in the currencies of the various members. The rest of the capital is to be called in only if needed to meet losses and must be paid in gold or American dollars or in the currency in which the obligation is to be met.

Designed for Specific Loans

The bank is designed to operate primarily by guaranteeing loans for specific projects such as railroads, harbor works and steel plants, although it may make such loans direct either out of its paid-in capital or from the proceeds of debentures which it may sell. If it borrows money, loans made with the proceeds of the borrowed money will be payable in the same currency as that borrowed by the bank. Of course, in the case of a loan guaranteed by the bank, the loan itself would be payable in the currency of the country from which the money was borrowed.

Every loan made must be for a specific project which has been investigated by the bank as to its desirability and which it is believed will increase the productive power of the borrowing country. Due regard is to be given to the ability of the country to service the interest and amortization charges on the loan.

Every loan must be guaranteed either by the national government of the country in which the project is located or by that country's central bank or some comparable institution. The bank will only make or guarantee loans for that portion of the cost of a project represented by imported material which has to be paid for in foreign exchange. The local expenditures on any project which can be met with the country's own currency must be raised by that country independently of the bank. For instance, if the bank made or guaranteed a loan to Brazil for the purpose of building a railroad, Brazil could borrow from the bank or under the bank's guarantee the money to pay for steel rails, locomotives, rolling stock, signal apparatus, etc., which would have to be imported. It would have to raise the money independently of the bank to pay the construction labor and to pay for the local materials used.

No loan can be raised by the bank or under its guarantee without the consent of the country in which the loan is raised or in whose currency it is payable. While this provision was inserted primarily for the purpose of enabling each country to protect its own money markets, it has the incidental effect of giving to the United States—the one country in which most of the loans made or guaranteed by the bank will have to be raised—a continuing veto power on the bank's operations.

The various provisions regarding the making of loans should prevent the improvident foreign lending which occurred in the 20's. A large portion of those loans was used to defray expenditures for which the money could and should have been raised locally and for purposes such as the construction of opera houses in Latin-America, planetariums in Germany, etc. Most of those loans were made without any consideration of the country's ability to provide the foreign exchange required to service them.

The amount of loans which the bank can make or guarantee is restricted to its unimpaired capital. If one assumes that one-half of all the money loaned or guaranteed by the bank was completely lost, an experience much worse than anything that has happened in the past in connection with foreign loans, and that only one-half of the various countries' subscriptions to the bank's capital are good, the holders of the bank's debentures or of obligations guaranteed by it would be assured of payment in full. If one considers that approximately one-third of the total capital is to be subscribed by the United States, 13 per cent by the United Kingdom, 3 per cent by Canada and almost equally large amounts by Holland and Belgium, it is most unlikely that over 50 per cent of the subscription calls would not be met. There is no practical possibility of countries like England and Canada themselves borrowing from the bank, as they could not be considered as either devastated or economically backward.

In conclusion, I can only state that no one thinks that either the fund or the bank, or both together, will be sufficient in itself to cure the evils of the world at the conclusion of the present war. They should, however, help tremendously toward restoring something like bearable economic conditions and reasonable stability throughout the world and in developing multilateral world trade. I am one of those who believes that the United States cannot in its own interest and with safety to itself remain isolated and apart from the rest of the world. If another world war should occur, we would not merely have another Pearl Harbor. Our industrial centers, such as Chicago and Pittsburgh, and vital communication and transportation facilities such as the Soo Locks would be largely destroyed before we would know what had happened. Apart from the question of military security, no considerable section of the world—not even the United States—can enjoy domestic prosperity if acute depression reigns throughout other large sections of the world. The two plans are not perfect. They both involve some element of risk of the money we put into them. But they represent not weeks but months and years of study and earnest effort, of collaboration and compromise made by different national interests to bring about the result which all the united and allied nations desire. I hope and I believe that the Congress of the United States will approve them.

(Copyright 1945 by COMMERCE Magazine, 1 N. La Salle St., Chicago, Ill.)

The Bretton Woods Plan To Prevent International Financial Chaos

By EDWARD E. BROWN
Board Chairman, First National Bank of Chicago

SPEECH OF THE MONTH

(Condensed)

Made before the Chicago Association of Commerce, January 17, 1945.

THE United Nations Monetary and Financial Conference, held at Bretton Woods, N. H., for three weeks in July, was attended by the representatives of 44 nations. The conference met on the invitation of the United States and was the outgrowth of a series of informal bilateral discussions, beginning almost 18 months before the conference met, between technicians of 30 different countries. The technical experts of a dozen or more of the larger and more important countries, including the United States, the United Kingdom and Russia, met at Atlantic City prior to the formal conference and discussed the matters to be considered by it. Nothing was settled at Atlantic City, but discussions there gave the principal countries concerned an understanding of each other's viewpoints and greatly facilitated the later work at Bretton Woods.

The conference produced two agreements for submission to the various governments represented, one providing for the formation of an international monetary fund and the other for an international bank for reconstruction and development. Each of the two organizations as proposed is distinct and separate from the other, and each has a different purpose although the two organizations supplement each other. The international monetary fund is designed to assist the various countries of the world in settling balances due on current accounts, to promote exchange stability, and thus to facilitate the extension of a balanced growth of international trade. The bank for reconstruction and development is designed to encourage the exportation of capital for productive purposes from countries like the U. S. which are in position to export capital to countries which need such capital either because they have been devastated by the war or because they are economically undeveloped. Both institutions represent a cooperative international effort to solve problems for the common benefit of all the nations of the world. The management of both institutions is to represent and to be elected by all the countries subscribing to them.

No participant in the conference or in the preliminary meeting of the experts could fail to be impressed by the real desire of all the United and Allied Nations to work together for the common good and in doing so to modify and compromise strongly held views and opinions. This is true of all the nations represented and not least of the two strongest nations after the United States, Russia and the United Kingdom. Both agreements as finally drafted necessarily represent compromises, as all international agreements must if the world is not to dominated by a single power. The smaller powers in many cases were represented by delegates of great ability and technical knowledge, and they made important contributions to the conference. Their points of view and special interests were always carefully considered and every effort was made by the conference to recognize them when it was possible to do so.

Currency Must Be Stable

Most of you, I am sure, recognize the fact that a country cannot create or maintain any considerable degree of internal economic activity without a currency in which its citizens have sufficient confidence to make them willing to take it in trade with each other and to make contracts running for at least short periods in terms of that currency. I am sure you also recognize that if trade is to be conducted between individuals of various countries and not through the medium of a state, or state-controlled companies, that the currencies of various countries must have at least relative stability in relation to each other.

Few of us, I think, realize how tremendous the instability of the currencies of many war-devastated countries and other countries not physically devastated, but whose economies have been disrupted by the war, will be when peace comes.

At the present time lend-lease and other devices give an artificial appearance of stability to many currencies. Once peace comes, unless something drastic is done to bring about currency stabilization, economic chaos is certain to result in many countries. Economic chaos means not only practically no international trade; it also means civil war and political unrest. Witness the recent case of Greece. Economic chaos in Europe would result in much of the continent either going communistic and tying itself up with Russia or trying some form of centralized state dictatorship of the type we are now fighting to destroy. In our own interest, not only because a good volume of foreign trade may mean the difference between reasonably full employment and depression at home but because of the greatly increased military and naval expenses to which we will be put if the rest of the world is in turmoil, it is imperative that we act to prevent postwar currency chaos from developing in the countries of the world.

The proposed international monetary fund is essentially a cooperative arrangement under which each country party to it agrees to make available to the other members an amount of its currency and gold equivalent to a given amount of American dollars, which amount is called that country's quota. In return, each country gets the right, subject to various limitations and conditions, to borrow money from the fund up to the amount of its quota for the purpose of paying for imports and balancing its international payments, but with the proviso that no country shall have the right to borrow more than 25 per cent of its quota in any one year. A country borrowing must pay interest at rates which increase progressively both with the length of time that the loan remains outstanding, and with the percentage of its quota borrowed.

One frequently heard criticism of the fund is that it is premature and that the world is not ready for it. Even with the

REPRINTED FROM COMMERCE MAGAZINE, FEBRUARY, 1945

recent military setbacks, it is possible that the occupied nations of Europe may soon all be liberated and major hostilities in Europe cease. If the nations of Europe are to get on their feet and are not to fall into chaos, it is necessary that at the earliest possible date they have currencies with some degree of stability and which can be recognized and used as a basis for international trade. It is almost equally necessary that many other countries, which were neither devastated nor occupied and which are exporters of foodstuffs and raw materials, but whose economies have suffered from the war, should also have national currencies with some stability if they are to export or import. While some degree of economic reconstruction and rebuilding of destroyed facilities for production and transport will have to be done in the countries which were occupied by the enemy before any considerable exports can be expected, this reconstruction will be slowed to a snail's pace if their people lack confidence in their domestic currencies. Reconstruction and currency confidence go together. To say that one must precede the other is like saying the egg must precede the hen. To say that currency stabilization must be preceded by economic reconstruction, balanced foreign trade, and balanced budgets is to put off the possibility of all these for at least a generation.

All the nations represented at Bretton Woods realized that no currency stabilization was possible in the case of a country which was engaged in civil war, or in major hostilities in its home area, or in which any considerable and unusual segment of its population was starving. On the other hand, the need of starting up international trade in Europe, South America, Africa, Australia and the Middle East is too urgent to wait until the Japanese war is finally over.

Regulations on Fund

The fund agreement provides that in no event shall the fund engage in exchange transactions until after major hostilities in Europe have ceased and, further, contains provisions designed to keep the fund from opening up its resources to a country engaged in civil war or to a country like China still fighting in its home area, or to one which has not passed the starvation stage which may in some countries temporarily follow this war.

It is also argued that the fund is too large for stabilization purposes and will therefore encourage countries to delay the necessary steps to balance their foreign payments. However, it should be realized that the dislocations in trade caused by the war will inevitably lead to much larger fluctuations in the exports and imports of many countries than would normally exist, and that the amounts required to offset disequilibriums in the balance of payments in the first few post-war years are greater than would normally be the case. If one keeps these facts in mind, the total amount of the fund ($8,800,000,000) and the quotas given the various countries of the world, including the United States with a quota of $2,750,000,000 and the United Kingdom with a quota of $1,300,000,000, do not generally appear to be too large.

Russia, with a complete system of state trade, does not require credit for strictly stabilization purposes, and it may be admitted that Russia will probably use up her quota in the first few years of the fund's existence to pay for imported capital goods necessary for her economic reconstruction. It must also be realized that once her economy is reconstructed Russia, with her large population, with an unquestionably stable government, whether one likes it or not, and with natural resources second only to those of the United States, will be in a position to repay her borrowings from the fund without difficulty.

Fund to Control Loans

It is difficult to see how any scheme for international stabilization of currencies could work with Russia not cooperating.

The most strongly urged criticism of the fund agreement is that it gives a country the right, subject to various restrictions and conditions, to borrow from the fund up to the amount of its quota.

It is argued by many that the fund should be the sole judge of the credit worthiness of countries desiring to use its resources and should have absolute discretion in the matter of granting or refusing credit. The proponents of this view say that it is impossible to conceive a sound credit organization operating on any other basis than the normal basis between lender and borrower in which the lender is the sole judge of the credit. It should be borne in mind that the fund is dealing with sovereign governments and their central banks which must know not only what their resources in hand are, but also what borrowing facilities they can count upon. A large corporation in this country whose operations may require it to use borrowed money almost always insists on its banks giving it lines of credit, which the corporation may not use, but which its management knows are available in case of need. Many large and very solvent corporations in recent years have gone further and are paying annual fees to banks in return for getting definite rights to borrow up to certain amounts over a term of years. The necessity of central banks and treasuries knowing definitely what reserve credit they can count upon is much greater than that of a business corporation.

The fund agreement recognizes this fact, but at the same time the right to draw upon the fund is a right subject to conditions, except as to initial borrowing which cannot exceed 25 per cent of a country's quota. If the fund finds that a country is using its borrowing power in a manner contrary to the purposes of the fund, it may limit further borrowings or declare the country ineligible to use the resources of the fund. Every country desiring to borrow from the fund, including its initial borrowings, must represent that it presently needs to borrow in order to make current payments which are consistent with the provisions of the agreement. And, the fund may postpone initial exchange transactions with a member country if it believes that country's condition is such that it cannot use the fund for the purposes for which it is intended, or except in a way prejudicial to the fund and its members.

Since voting rights in the fund and control of its management are closely related to the quotas of various countries and since the United States has the largest quota I think it can reasonably be assumed that the American viewpoint will dominate the management of the fund. Furthermore, if, as is certain to be the case, the American dollar is the currency most in demand after the war the knowledge on the part of other countries that the United States can withdraw if its viewpoint is flouted by the management should practically insure recognition of our views by the fund.

Changes in Currency Value

The fund is not intended to set up a fixed gold standard and tie all the currencies of the world to gold. Few, if any, countries in the world consider such a tie-up desirable. Many, probably most countries, feel today that circumstances may arise which would make a change in the gold value of their currency imperative. But the fund does make such changes more difficult, and does ensure that they will not be undertaken lightly. In the first place, every country must consult with the fund before making a change. In the second place, it must make up any reduction in the gold value of its currency held by the fund. After initial changes aggregating, up and down, a total of not more than ten percent, the fund may object to a proposed change, and if the country over the fund's objection changes the par value of its currency, it loses its right to borrow from the fund. To be sure, it is provided that the fund shall concur in a proposed change if it is satisfied that it is necessary to correct a fundamental disequilibrium, and it shall not

object to a change because of the domestic social or political policies of a member country. It is unlikely, in view of these provisions, that in the case of any first class power the fund would refuse its consent to a change in the gold value of a currency if after discussion and argument that power insisted on its necessity. But a great power rarely changes the gold parity of its currency, in peace time at least, unless forced to do so by prior changes in the parity of the currencies of other countries which upset the relative value of its currency in international transactions.

The fund would make gold the index of the value of a currency and would maintain the use of gold for the settlement of international balances. By so doing it would exercise a strong psychological influence on all countries to maintain the gold value of their currencies. Various countries at Bretton Woods argued that the fund was too much of a gold standard plan, and most of the attacks upon it in England are based upon the fact that it will make changes in the gold value of sterling too difficult. As a compromise between rigidity and flexibility the very fact that the fund is being attacked both because it ties currencies too rigidly and too flexibly to gold indicates that it is probably as fair a compromise between two points of view as could be obtained.

In spite of the fact that the fund provides for changes in the gold value of a currency and that many such changes may be made under its terms, the fund should accomplish three very desirable results: first, end the nuisance of multiple currencies after the transition period; second, do away with competitive exchange depreciation; and, third, prevent the use of currency manipulation and depreciation for predatory political and economic purposes. Germany showed the danger to the world of allowing currency manipulation for such purposes.

Eliminate Exchange Restrictions

The fund is designed primarily to facilitate international payments on current account only, and its credit facilities are limited to this purpose. It had to be recognized that the postwar period is going to be one of great difficulty and transition and that exchange controls even for payments on current account established during the war cannot be eliminated at once. No one can say how long the transitional period will last, but it is certain to be a matter of years. The fund does provide that member countries shall take all possible measures, as soon as conditions permit, to facilitate international payments and progressively to do away with present exchange restrictions. It must be admitted that the teeth given the fund to enforce the withdrawal of restrictions on current payments now in effect are weak. But, realistically, one must remember that the maintenance of many of these restrictions for some years after peace is necessary to the economic survival of various nations, and that nations are sovereign and are naturally and properly very jealous of their rights when a question of their economic survival is at stake.

Chief Objection to Plan

The objection to the fund which has the greatest popular appeal in this country is the one that except for relatively small contributions of gold by other countries the United States is allegedly the only country which will put up currency that will be really in demand. Although the American dollar will be the currency most in demand, the currencies of other countries able to export large amounts of raw materials are also certain to be in demand. Canada, Cuba and other Latin American countries are certain to be in this category. There will be a considerable demand for sterling. The fund will have a very considerable amount of gold contributed by countries other than the United States. Many countries have large gold holdings and dollar balances which they will presumably use before drawing on the fund. The fund agreement provides that as the gold holdings or holdings of American dollars of a country increase it must repay part of its borrowings from the fund.

Bearing these facts in mind and also the fact that no country has the right to draw more than 25 percent of its quota in any one year, the dollars and gold in the fund cannot under the most unfavorable circumstances become exhausted as rapidly as the objectors to the plan fear. If the United States recognizes the fundamental truth that a creditor nation must ultimately accept payment for its exports in goods, using the word "goods" to include services, the fund should be able to work indefinitely without the dollar becoming scarce. If the United States insists on continuing to export more than it imports, dollars are bound ultimately to become scarce and other countries of the world will have to discriminate against American goods no matter how much they may desire them. We can postpone that time by accepting gold or loaning money abroad. But ultimately we shall get all the gold with which the rest of the world is willing to part, and we shall become tired of loaning money for the purpose of enabling borrowers to pay for goods which we currently export, as well as interest on the money they have already borrowed.

It is to be hoped that before the dollars in the fund have become scarce the American people will have to come to a greater maturity in their economic thinking and will radically change their present tariff policy.

While it would be highly undesirable to have the American dollar declared scarce and exchange restrictions imposed against it by other countries, it should be realized that if nothing is done the dollar is bound to become generally scarce throughout the world in short order and existing exchange discriminations against it are certain to increase.

Even though the dollar is declared scarce and remains so, our contribution to the fund would not be lost. It would be frozen, to be sure, and we would lose interest on our contribution. But, barring another general world war, we could, over a period of years, convert our claim against the currencies of most of the nations held by the fund into goods and thus get most of our money back. The fund would still continue to function and the currencies of other countries would continue to be interchangeable at the parities fixed from time to time by the fund even though not convertible into dollars. This would benefit international trade and thus our own trade. Meanwhile, by our contribution to the fund we would have made possible currency stabilization in war-devasted countries and by thus helping them restore their economics we would greatly increase the chance of political stability, without which there is no chance for peace and general multilateral trade. And without these there cannot be continuing world prosperity or prosperity in this country.

U. S. Must Aid Nations

All the critics of the international monetary fund realize that the United States must in its own interest help the rest of the world get on its feet after this war is over either by gifts or by furnishing credit and taking credit risks. No proponent of the fund believes that it is a panacea, or that alone it will be sufficient to solve the economic problems of the world. Some considerable degree of currency stabilization is generally recognized as one of the indispensable things which must be provided for a reconstructed world economy.

No other plan has been suggested which involves less risk to the American people than the fund, even assuming that we still continue indefinitely our present high tariff policy.

The other plan drawn up at Bretton Woods is that of the international bank for reconstruction and development. The argument for such an institution is based on two premises, both of which I believe to be sound. The first premise is that the export of capital by a country like the United States, which is in a position to do so, to countries which have been devastated by the war or are economically undeveloped and can pro-

fitably use such capital, is a benefit not only to the particular exporting and importing countries but also to the other trading nations of the world. The second premise is that after the experience of the 20's and 30's with foreign loans no considerable amount of money will be loaned abroad, by Americans at least, at reasonable rates of interest except under some adequate governmental guarantee. At the present time, for certain classes of loans the export-import bank does give such a guarantee.

Since, however, the export of surplus capital by a country benefits not only itself and the receiving country but also all the other trading nations of the world, it is only fair that the risk involved in such lending should be shared by all such countries and not borne entirely by the exporting country.

The proposed bank developed at Bretton Woods will have a subscribed capital of $10,000,000,000, of which the United States' subscription is $3,175,000,000. The subscriptions of other countries generally correspond to their quotas in the international monetary fund. The bank will be governed by a board of directors representing the various countries, and the voting rights of these directors closely correspond with the subscriptions to the capital stock of the countries which elect them. As in the case of the fund, this means that the United States, plus a few countries whose economic thinking is like ours, will at all times be in control.

Twenty per cent of the bank's initial capital is to be paid in, one-tenth in gold or United States dollars and the balance in the currencies of the various members. The rest of the capital is to be called in only if needed to meet losses and must be paid in gold or American dollars or in the currency in which the obligation is to be met.

Designed for Specific Loans

The bank is designed to operate primarily by guaranteeing loans for specific projects such as railroads, harbor works and steel plants, although it may make such loans direct either out of its paid-in capital or from the proceeds of debentures which it may sell. If it borrows money, loans made with the proceeds of the borrowed money will be payable in the same currency as that borrowed by the bank. Of course, in the case of a loan guaranteed by the bank, the loan itself would be payable in the currency of the country from which the money was borrowed.

Every loan made must be for a specific project which has been investigated by the bank as to its desirability and which it is believed will increase the productive power of the borrowing country. Due regard is to be given to the ability of the country to service the interest and amortization charges on the loan.

Every loan must be guaranteed either by the national government of the country in which the project is located or by that country's central bank or some comparable institution. The bank will only make or guarantee loans for that portion of the cost of a project represented by imported material which has to be paid for in foreign exchange. The local expenditures on any project which can be met with the country's own currency must be raised by that country independently of the bank. For instance, if the bank made or guaranteed a loan to Brazil for the purpose of building a railroad, Brazil could borrow from the bank or under the bank's guarantee the money to pay for steel rails, locomotives, rolling stock, signal apparatus, etc., which would have to be imported. It would have to raise the money independently of the bank to pay the construction labor and to pay for the local materials used.

No loan can be raised by the bank or under its guarantee without the consent of the country in which the loan is raised or in whose currency it is payable. While this provision was inserted primarily for the purpose of enabling each country to protect its own money markets, it has the incidental effect of giving to the United States—the one country in which most of the loans made or guaranteed by the bank will have to be raised—a continuing veto power on the bank's operations.

The various provisions regarding the making of loans should prevent the improvident foreign lending which occurred in the 20's. A large portion of those loans was used to defray expenditures for which the money could and should have been raised locally and for purposes such as the construction of opera houses in Latin-America, planetariums in Germany, etc. Most of those loans were made without any consideration of the country's ability to provide the foreign exchange required to service them.

The amount of loans which the bank can make or guarantee is restricted to its unimpaired capital. If one assumes that one-half of all the money loaned or guaranteed by the bank was completely lost, an experience much worse than anything that has happened in the past in connection with foreign loans, and that only one-half of the various countries' subscriptions to the bank's capital are good, the holders of the bank's debentures or of obligations guaranteed by it would be assured of payment in full. If one considers that approximately one-third of the total capital is to be subscribed by the United States, 13 per cent by the United Kingdom, 3 per cent by Canada and almost equally large amounts by Holland and Belgium, it is most unlikely that over 50 per cent of the subscription calls would not be met. There is no practical possibility of countries like England and Canada themselves borrowing from the bank, as they could not be considered as either devastated or economically backward.

In conclusion, I can only state that no one thinks that either the fund or the bank, or both together, will be sufficient in itself to cure the evils of the world at the conclusion of the present war. They should, however, help tremendously toward restoring something like bearable economic conditions and reasonable stability throughout the world and in developing multilateral world trade. I am one of those who believes that the United States cannot in its own interest and with safety to itself remain isolated and apart from the rest of the world. If another world war should occur, we would not merely have another Pearl Harbor. Our industrial centers, such as Chicago and Pittsburgh, and vital communication and transportation facilities such as the Soo Locks would be largely destroyed before we would know what had happened. Apart from the question of military security, no considerable section of the world—not even the United States—can enjoy domestic prosperity if acute depression reigns throughout other large sections of the world. The two plans are not perfect. They both involve some element of risk of the money we put into them. But they represent not weeks but months and years of study and earnest effort, of collaboration and compromise made by different national interests to bring about the result which all the united and allied nations desire. I hope and I believe that the Congress of the United States will approve them.

(Copyright 1945 by COMMERCE Magazine, 1 N. La Salle St., Chicago, Ill.)

The Bretton Woods Plan To Prevent International Financial Chaos

By EDWARD E. BROWN
Board Chairman, First National Bank of Chicago

SPEECH OF THE MONTH

(Condensed)

Made before the Chicago Association of Commerce, January 17, 1945.

THE United Nations Monetary and Financial Conference, held at Bretton Woods, N. H., for three weeks in July, was attended by the representatives of 44 nations. The conference met on the invitation of the United States and was the outgrowth of a series of informal bilateral discussions, beginning almost 18 months before the conference met, between technicians of 30 different countries. The technical experts of a dozen or more of the larger and more important countries, including the United States, the United Kingdom and Russia, met at Atlantic City prior to the formal conference and discussed the matters to be considered by it. Nothing was settled at Atlantic City, but discussions there gave the principal countries concerned an understanding of each other's viewpoints and greatly facilitated the later work at Bretton Woods.

The conference produced two agreements for submission to the various governments represented, one providing for the formation of an international monetary fund and the other for an international bank for reconstruction and development. Each of the two organizations as proposed is distinct and separate from the other, and each has a different purpose although the two organizations supplement each other. The international monetary fund is designed to assist the various countries of the world in settling balances due on current accounts, to promote exchange stability, and thus to facilitate the extension of a balanced growth of international trade. The bank for reconstruction and development is designed to encourage the exportation of capital for productive purposes from countries like the U. S. which are in position to export capital to countries which need such capital either because they have been devastated by the war or because they are economically undeveloped. Both institutions represent a cooperative international effort to solve problems for the common benefit of all the nations of the world. The management of both institutions is to represent and to be elected by all the countries subscribing to them.

No participant in the conference or in the preliminary meeting of the experts could fail to be impressed by the real desire of all the United and Allied Nations to work together for the common good and in doing so to modify and compromise strongly held views and opinions. This is true of all the nations represented and not least of the two strongest nations after the United States, Russia and the United Kingdom. Both agreements as finally drafted necessarily represent compromises, as all international agreements must if the world is not to dominated by a single power. The smaller powers in many cases were represented by delegates of great ability and technical knowledge, and they made important contributions to the conference. Their points of view and special interests were always carefully considered and every effort was made by the conference to recognize them when it was possible to do so.

Currency Must Be Stable

Most of you, I am sure, recognize the fact that a country cannot create or maintain any considerable degree of internal economic activity without a currency in which its citizens have sufficient confidence to make them willing to take it in trade with each other and to make contracts running for at least short periods in terms of that currency. I am sure you also recognize that if trade is to be conducted between individuals of various countries and not through the medium of a state, or state-controlled companies, that the currencies of various countries must have at least relative stability in relation to each other.

Few of us, I think, realize how tremendous the instability of the currencies of many war-devastated countries and other countries not physically devastated, but whose economies have been disrupted by the war, will be when peace comes.

At the present time lend-lease and other devices give an artificial appearance of stability to many currencies. Once peace comes, unless something drastic is done to bring about currency stabilization, economic chaos is certain to result in many countries. Economic chaos means not only practically no international trade; it also means civil war and political unrest. Witness the recent case of Greece. Economic chaos in Europe would result in much of the continent either going communistic and tying itself up with Russia or trying some form of centralized state dictatorship of the type we are now fighting to destroy. In our own interest, not only because a good volume of foreign trade may mean the difference between reasonably full employment and depression at home but because of the greatly increased military and naval expenses to which we will be put if the rest of the world is in turmoil, it is imperative that we act to prevent postwar currency chaos from developing in the countries of the world.

The proposed international monetary fund is essentially a cooperative arrangement under which each country party to it agrees to make available to the other members an amount of its currency and gold equivalent to a given amount of American dollars, which amount is called that country's quota. In return, each country gets the right, subject to various limitations and conditions, to borrow money from the fund up to the amount of its quota for the purpose of paying for imports and balancing its international payments, but with the proviso that no country shall have the right to borrow more than 25 per cent of its quota in any one year. A country borrowing must pay interest at rates which increase progressively both with the length of time that the loan remains outstanding, and with the percentage of its quota borrowed.

One frequently heard criticism of the fund is that it is premature and that the world is not ready for it. Even with the

REPRINTED FROM COMMERCE MAGAZINE, FEBRUARY, 1945

recent military setbacks, it is possible that the occupied nations of Europe may soon all be liberated and major hostilities in Europe cease. If the nations of Europe are to get on their feet and are not to fall into chaos, it is necessary that at the earliest possible date they have currencies with some degree of stability and which can be recognized and used as a basis for international trade. It is almost equally necessary that many other countries, which were neither devastated nor occupied and which are exporters of foodstuffs and raw materials, but whose economies have suffered from the war, should also have national currencies with some stability if they are to export or import. While some degree of economic reconstruction and rebuilding of destroyed facilities for production and transport will have to be done in the countries which were occupied by the enemy before any considerable exports can be expected, this reconstruction will be slowed to a snail's pace if their people lack confidence in their domestic currencies. Reconstruction and currency confidence go together. To say that one must precede the other is like saying the egg must precede the hen. To say that currency stabilization must be preceded by economic reconstruction, balanced foreign trade, and balanced budgets is to put off the possibility of all these for at least a generation.

All the nations represented at Bretton Woods realized that no currency stabilization was possible in the case of a country which was engaged in civil war, or in major hostilities in its home area, or in which any considerable and unusual segment of its population was starving. On the other hand, the need of starting up international trade in Europe, South America, Africa, Australia and the Middle East is too urgent to wait until the Japanese war is finally over.

Regulations on Fund

The fund agreement provides that in no event shall the fund engage in exchange transactions until after major hostilities in Europe have ceased and, further, contains provisions designed to keep the fund from opening up its resources to a country engaged in civil war or to a country like China still fighting in its home area, or to one which has not passed the starvation stage which may in some countries temporarily follow this war.

It is also argued that the fund is too large for stabilization purposes and will therefore encourage countries to delay the necessary steps to balance their foreign payments. However, it should be realized that the dislocations in trade caused by the war will inevitably lead to much larger fluctuations in the exports and imports of many countries than would normally exist, and that the amounts required to offset disequilibriums in the balance of payments in the first few post-war years are greater than would normally be the case. If one keeps these facts in mind, the total amount of the fund ($8,800,000,000) and the quotas given the various countries of the world, including the United States with a quota of $2,750,000,000 and the United Kingdom with a quota of $1,300,000,000, do not generally appear to be too large.

Russia, with a complete system of state trade, does not require credit for strictly stabilization purposes, and it may be admitted that Russia will probably use up her quota in the first few years of the fund's existence to pay for imported capital goods necessary for her economic reconstruction. It must also be realized that once her economy is reconstructed Russia, with her large population, with an unquestionably stable government, whether one likes it or not, and with natural resources second only to those of the United States, will be in a position to repay her borrowings from the fund without difficulty.

Fund to Control Loans

It is difficult to see how any scheme for international stabilization of currencies could work with Russia not cooperating.

The most strongly urged criticism of the fund agreement is that it gives a country the right, subject to various restrictions and conditions, to borrow from the fund up to the amount of its quota.

It is argued by many that the fund should be the sole judge of the credit worthiness of countries desiring to use its resources and should have absolute discretion in the matter of granting or refusing credit. The proponents of this view say that it is impossible to conceive a sound credit organization operating on any other basis than the normal basis between lender and borrower in which the lender is the sole judge of the credit. It should be borne in mind that the fund is dealing with sovereign governments and their central banks which must know not only what their resources in hand are, but also what borrowing facilities they can count upon. A large corporation in this country whose operations may require it to use borrowed money almost always insists on its banks giving it lines of credit, which the corporation may not use, but which its management knows are available in case of need. Many large and very solvent corporations in recent years have gone further and are paying annual fees to banks in return for getting definite rights to borrow up to certain amounts over a term of years. The necessity of central banks and treasuries knowing definitely what reserve credit they can count upon is much greater than that of a business corporation.

The fund agreement recognizes this fact, but at the same time the right to draw upon the fund is a right subject to conditions, except as to initial borrowing which cannot exceed 25 per cent of a country's quota. If the fund finds that a country is using its borrowing power in a manner contrary to the purposes of the fund, it may limit further borrowings or declare the country ineligible to use the resources of the fund. Every country desiring to borrow from the fund, including its initial borrowings, must represent that it presently needs to borrow in order to make current payments which are consistent with the provisions of the agreement. And, the fund may postpone initial exchange transactions with a member country if it believes that country's condition is such that it cannot use the fund for the purposes for which it is intended, or except in a way prejudicial to the fund and its members.

Since voting rights in the fund and control of its management are closely related to the quotas of various countries and since the United States has the largest quota I think it can reasonably be assumed that the American viewpoint will dominate the management of the fund. Furthermore, if, as is certain to be the case, the American dollar is the currency most in demand after the war the knowledge on the part of other countries that the United States can withdraw if its viewpoint is flouted by the management should practically insure recognition of our views by the fund.

Changes in Currency Value

The fund is not intended to set up a fixed gold standard and tie all the currencies of the world to gold. Few, if any, countries in the world consider such a tie-up desirable. Many, probably most countries, feel today that circumstances may arise which would make a change in the gold value of their currency imperative. But the fund does make such changes more difficult, and does ensure that they will not be undertaken lightly. In the first place, every country must consult with the fund before making a change. In the second place, it must make up any reduction in the gold value of its currency held by the fund. After initial changes aggregating, up and down, a total of not more than ten percent, the fund may object to a proposed change, and if the country over the fund's objection changes the par value of its currency, it loses its right to borrow from the fund. To be sure, it is provided that the fund shall concur in a proposed change if it is satisfied that it is necessary to correct a fundamental disequilibrium, and it shall not

object to a change because of the domestic social or political policies of a member country. It is unlikely, in view of these provisions, that in the case of any first class power the fund would refuse its consent to a change in the gold value of a currency if after discussion and argument that power insisted on its necessity. But a great power rarely changes the gold parity of its currency, in peace time at least, unless forced to do so by prior changes in the parity of the currencies of other countries which upset the relative value of its currency in international transactions.

The fund would make gold the index of the value of a currency and would maintain the use of gold for the settlement of international balances. By so doing it would exercise a strong psychological influence on all countries to maintain the gold value of their currencies. Various countries at Bretton Woods argued that the fund was too much of a gold standard plan, and most of the attacks upon it in England are based upon the fact that it will make changes in the gold value of sterling too difficult. As a compromise between rigidity and flexibility the very fact that the fund is being attacked both because it ties currencies too rigidly and too flexibly to gold indicates that it is probably as fair a compromise between two points of view as could be obtained.

In spite of the fact that the fund provides for changes in the gold value of a currency and that many such changes may be made under its terms, the fund should accomplish three very desirable results: first, end the nuisance of multiple currencies after the transition period; second, do away with competitive exchange depreciation; and, third, prevent the use of currency manipulation and depreciation for predatory political and economic purposes. Germany showed the danger to the world of allowing currency manipulation for such purposes.

Eliminate Exchange Restrictions

The fund is designed primarily to facilitate international payments on current account only, and its credit facilities are limited to this purpose. It had to be recognized that the postwar period is going to be one of great difficulty and transition and that exchange controls even for payments on current account established during the war cannot be eliminated at once. No one can say how long the transitional period will last, but it is certain to be a matter of years. The fund does provide that member countries shall take all possible measures, as soon as conditions permit, to facilitate international payments and progressively to do away with present exchange restrictions. It must be admitted that the teeth given the fund to enforce the withdrawal of restrictions on current payments now in effect are weak. But, realistically, one must remember that the maintenance of many of these restrictions for some years after peace is necessary to the economic survival of various nations, and that nations are sovereign and are naturally and properly very jealous of their rights when a question of their economic survival is at stake.

Chief Objection to Plan

The objection to the fund which has the greatest popular appeal in this country is the one that except for relatively small contributions of gold by other countries the United States is allegedly the only country which will put up currency that will be really in demand. Although the American dollar will be the currency most in demand, the currencies of other countries able to export large amounts of raw materials are also certain to be in demand. Canada, Cuba and other Latin American countries are certain to be in this category. There will be a considerable demand for sterling. The fund will have a very considerable amount of gold contributed by countries other than the United States. Many countries have large gold holdings and dollar balances which they will presumably use before drawing on the fund. The fund agreement provides that as the gold holdings or holdings of American dollars of a country increase it must repay part of its borrowings from the fund.

Bearing these facts in mind and also the fact that no country has the right to draw more than 25 percent of its quota in any one year, the dollars and gold in the fund cannot under the most unfavorable circumstances become exhausted as rapidly as the objectors to the plan fear. If the United States recognizes the fundamental truth that a creditor nation must ultimately accept payment for its exports in goods, using the word "goods" to include services, the fund should be able to work indefinitely without the dollar becoming scarce. If the United States insists on continuing to export more than it imports, dollars are bound ultimately to become scarce and other countries of the world will have to discriminate against American goods no matter how much they may desire them. We can postpone that time by accepting gold or loaning money abroad. But ultimately we shall get all the gold with which the rest of the world is willing to part, and we shall become tired of loaning money for the purpose of enabling borrowers to pay for goods which we currently export, as well as interest on the money they have already borrowed.

It is to be hoped that before the dollars in the fund have become scarce the American people will have to come to a greater maturity in their economic thinking and will radically change their present tariff policy.

While it would be highly undesirable to have the American dollar declared scarce and exchange restrictions imposed against it by other countries, it should be realized that if nothing is done the dollar is bound to become generally scarce throughout the world in short order and existing exchange discriminations against it are certain to increase.

Even though the dollar is declared scarce and remains so, our contribution to the fund would not be lost. It would be frozen, to be sure, and we would lose interest on our contribution. But, barring another general world war, we could, over a period of years, convert our claim against the currencies of most of the nations held by the fund into goods and thus get most of our money back. The fund would still continue to function and the currencies of other countries would continue to be interchangeable at the parities fixed from time to time by the fund even though not convertible into dollars. This would benefit international trade and thus our own trade. Meanwhile, by our contribution to the fund we would have made possible currency stabilization in war-devasted countries and by thus helping them restore their economics we would greatly increase the chance of political stability, without which there is no chance for peace and general multilateral trade. And without these there cannot be continuing world prosperity or prosperity in this country.

U. S. Must Aid Nations

All the critics of the international monetary fund realize that the United States must in its own interest help the rest of the world get on its feet after this war is over either by gifts or by furnishing credit and taking credit risks. No proponent of the fund believes that it is a panacea, or that alone it will be sufficient to solve the economic problems of the world. Some considerable degree of currency stabilization is generally recognized as one of the indispensable things which must be provided for a reconstructed world economy.

No other plan has been suggested which involves less risk to the American people than the fund, even assuming that we still continue indefinitely our present high tariff policy.

The other plan drawn up at Bretton Woods is that of the international bank for reconstruction and development. The argument for such an institution is based on two premises, both of which I believe to be sound. The first premise is that the export of capital by a country like the United States, which is in a position to do so, to countries which have been devastated by the war or are economically undeveloped and can pro-

fitably use such capital, is a benefit not only to the particular exporting and importing countries but also to the other trading nations of the world. The second premise is that after the experience of the 20's and 30's with foreign loans no considerable amount of money will be loaned abroad, by Americans at least, at reasonable rates of interest except under some adequate governmental guarantee. At the present time, for certain classes of loans the export-import bank does give such a guarantee.

Since, however, the export of surplus capital by a country benefits not only itself and the receiving country but also all the other trading nations of the world, it is only fair that the risk involved in such lending should be shared by all such countries and not borne entirely by the exporting country.

The proposed bank developed at Bretton Woods will have a subscribed capital of $10,000,000,000, of which the United States' subscription is $3,175,000,000. The subscriptions of other countries generally correspond to their quotas in the international monetary fund. The bank will be governed by a board of directors representing the various countries, and the voting rights of these directors closely correspond with the subscriptions to the capital stock of the countries which elect them. As in the case of the fund, this means that the United States, plus a few countries whose economic thinking is like ours, will at all times be in control.

Twenty per cent of the bank's initial capital is to be paid in, one-tenth in gold or United States dollars and the balance in the currencies of the various members. The rest of the capital is to be called in only if needed to meet losses and must be paid in gold or American dollars or in the currency in which the obligation is to be met.

Designed for Specific Loans

The bank is designed to operate primarily by guaranteeing loans for specific projects such as railroads, harbor works and steel plants, although it may make such loans direct either out of its paid-in capital or from the proceeds of debentures which it may sell. If it borrows money, loans made with the proceeds of the borrowed money will be payable in the same currency as that borrowed by the bank. Of course, in the case of a loan guaranteed by the bank, the loan itself would be payable in the currency of the country from which the money was borrowed.

Every loan made must be for a specific project which has been investigated by the bank as to its desirability and which it is believed will increase the productive power of the borrowing country. Due regard is to be given to the ability of the country to service the interest and amortization charges on the loan.

Every loan must be guaranteed either by the national government of the country in which the project is located or by that country's central bank or some comparable institution. The bank will only make or guarantee loans for that portion of the cost of a project represented by imported material which has to be paid for in foreign exchange. The local expenditures on any project which can be met with the country's own currency must be raised by that country independently of the bank. For instance, if the bank made or guaranteed a loan to Brazil for the purpose of building a railroad, Brazil could borrow from the bank or under the bank's guarantee the money to pay for steel rails, locomotives, rolling stock, signal apparatus, etc., which would have to be imported. It would have to raise the money independently of the bank to pay the construction labor and to pay for the local materials used.

No loan can be raised by the bank or under its guarantee without the consent of the country in which the loan is raised or in whose currency it is payable. While this provision was inserted primarily for the purpose of enabling each country to protect its own money markets, it has the incidental effect of giving to the United States—the one country in which most of the loans made or guaranteed by the bank will have to be raised—a continuing veto power on the bank's operations.

The various provisions regarding the making of loans should prevent the improvident foreign lending which occurred in the 20's. A large portion of those loans was used to defray expenditures for which the money could and should have been raised locally and for purposes such as the construction of opera houses in Latin-America, planetariums in Germany, etc. Most of those loans were made without any consideration of the country's ability to provide the foreign exchange required to service them.

The amount of loans which the bank can make or guarantee is restricted to its unimpaired capital. If one assumes that one-half of all the money loaned or guaranteed by the bank was completely lost, an experience much worse than anything that has happened in the past in connection with foreign loans, and that only one-half of the various countries' subscriptions to the bank's capital are good, the holders of the bank's debentures or of obligations guaranteed by it would be assured of payment in full. If one considers that approximately one-third of the total capital is to be subscribed by the United States, 13 per cent by the United Kingdom, 3 per cent by Canada and almost equally large amounts by Holland and Belgium, it is most unlikely that over 50 per cent of the subscription calls would not be met. There is no practical possibility of countries like England and Canada themselves borrowing from the bank, as they could not be considered as either devastated or economically backward.

In conclusion, I can only state that no one thinks that either the fund or the bank, or both together, will be sufficient in itself to cure the evils of the world at the conclusion of the present war. They should, however, help tremendously toward restoring something like bearable economic conditions and reasonable stability throughout the world and in developing multilateral world trade. I am one of those who believes that the United States cannot in its own interest and with safety to itself remain isolated and apart from the rest of the world. If another world war should occur, we would not merely have another Pearl Harbor. Our industrial centers, such as Chicago and Pittsburgh, and vital communication and transportation facilities such as the Soo Locks would be largely destroyed before we would know what had happened. Apart from the question of military security, no considerable section of the world—not even the United States—can enjoy domestic prosperity if acute depression reigns throughout other large sections of the world. The two plans are not perfect. They both involve some element of risk of the money we put into them. But they represent not weeks but months and years of study and earnest effort, of collaboration and compromise made by different national interests to bring about the result which all the united and allied nations desire. I hope and I believe that the Congress of the United States will approve them.

(Copyright 1945 by COMMERCE Magazine, 1 N. La Salle St., Chicago, Ill.)