PRESS REPORTS

The Economist
London
September 29, 1962

EUROPE AND THE MONEY DEADLOCK

Will the deadlock over reform of the system of international payments soon be broken by the natural development of a new monetary power, a European Economic Community that includes Britain? Mr. Robert Roosa, chief policy maker for the dollar, is now hinting that it will, and is thereby glossing over the disagreements over the immediate way ahead that opened up between the United States and Britain at last week's meeting of the International Monetary Fund in Washington. The financial consequences of Britain joining the European common market are indeed intriguing, and deserve more intensive study than they have received so far. Unfortunately they are also, for the immediate future, especially while Britain's entry is in the balance, incalculable; one can consider the consequences of various lines of development, but only guess at which line may be chosen. So if one is worried that the present system of international finance may be a handicap to world economic expansion in 1963 and 1964, the thought of how the common market may have changed that system by 1970 is not very relevant.

The American dismissal of Mr. Maudling's tentative and deliberately flexible plan for a new mutual currency account in the IMF, described in these columns last week, is therefore disappointing, and one fears that Mr. Roosa's tactics, which have been broadly commendable hitherto, may now be going seriously wrong. The most disquieting element in the American attitude in the past fortnight, exemplified from President Kennedy downward, has been obsession with prestige--that notoriously dangerous intruder into the currency arena. The American authorities appear to be reverting to the <u>tout va bien</u> mentality of their Republican predecessors. Any implication, even in so mild a form as that in the Maudling plan, that the reserve currency system may have possible limits and may therefore need to be supplemented in a small way by a new and international form of credit is taken as a slight on the dollar. The dollar, it is held, remains fully capable of supplementing gold as a means of payment, and, with the help of the innovations begun over the past eighteen months as a small beginning to the cross-holding of currencies, it will be adequate for the next five years, if not ten--by when a new key currency will have emerged from the new European grouping. Throughout this American discussion there is a curious and psychologically harmful reluctance even to mention that there is another currency, which Mr. Maudling probably had in mind, which fulfils a reserve currency function right now.

These petty irritations produced by myopic thinking on national lines could prove unfortunate for the American Treasury; for Mr. Roosa, in his own schemes, is dependent on international support and co-operation. The British Treasury almost certainly made a considerable (if politically explicable) mistake in not producing its initiative for free discussion with the Americans at a much earlier point this year, before Mr. Roosa's own conceptions had hardened. But now Britain has produced a scheme that can be run perfectly well alongside Mr. Roosa's. Thus countries that wish to accumulate national currencies in their reserves can still do so, à la Roosa; while those that prefer to hold a part of their accumulations in a claim on IMF, à la Maudling, can do that. The particular American objection to the Maudling scheme, its provision for a gold value guarantee on these (like all existing) claims on IMF, is not well founded; under the limited arrangement which Britain is now suggesting it would not be possible, as the Americans fear, for countries to turn existing dollar balances into guaranteed deposits with IMF (though what a good idea that would be!).

The American position on guarantees is, in fact, incompatible with Mr. Roosa's own aims. How does he expect to get his mutual holding of currencies moving without them? Suppose the United States payments balance remains in net deficit. Are other countries to be persuaded to increase their holdings of dollars in ordinary forms? The American authorities know that dollar holdings of countries like Switzerland have to be guaranteed in effect (as was recently done through the bilateral swap arrangements); and what hope have they of getting Britain to hold entirely unguaranteed dollars at this stage? But suppose, as the American authorities hope, that the American payments balance swings into surplus. Mr. Roosa has intimated that his surplus will be taken in European currencies, and this would indeed be an important relief for world liquidity. Does Mr. Roosa really intend to build up billions of dollars worth of pounds, marks, francs and lire--all unguaranteed? American objections to guarantees are closely connected with fears of trouble with Congress. What are senators expected to say about Uncle Sam standing at large risk on currencies they can barely pronounce?

In practice this regrettable and largely artificial division between the United States and Britain on their common problem--how to provide adequate international leeway for speedier domestic growth--is likely to mean that neither scheme will make any substantial progress until attitudes change. Mr. Maudling, returning to his weak domestic economy, can only be advised to drive on as intended--and fasten his international safety belt. One hopes that the same will be done by his American counterparts. For the short term, existing lines of credit in IMF and elsewhere are very likely sufficient to take care of the pound or the dollar, whichever should need aid next; and one has just got to take the risk that they are not. Before very long, unless all the hopes of western economic progress in the sixties are to be discarded, the American attitude will surely change. And a change in attitudes in continental Europe could come about in the context of its own scheme within the common market.

This is the point at which Mr. Roosa may have been groping. But even here no quick results are to be expected. A new reserve currency managed by the common market would entail a pooling of reserves among individual countries in a central reserve union. This was proposed some time ago by

M. Monnet's action group. The proposal received a dusty reception among national financial officials. Finance is regarded as the end-process of integration, and practice in the common market so far has certainly not run ahead of the modest stipulations set down in the treaty. There is, also, a particular difficulty about a reserve pool. The contrasting relations between reserves and liabilities in Britain on the one hand and in continental countries on the other makes any proposal for integration appear neat to the reformer but lop-sided to the banker--as a sharing, as one French official bluntly put it to an English visitor, "of our money and your debts."

This is a big hurdle; but it has recently been suggested that it can be by-passed. M. Raymond Bertrand, deputy director of trade and payments at the Organisation for Economic Co-operation and Development, has proposed that a European institution should be empowered to create credit and deposits which would be available for settlement between central banks in the common market--but could not be exchanged for gold and convertible currencies. "Thus the issuing institution would not have to hold reserves or concern itself with liquidity in the technical sense of the term. . . . The deposits created by a common European institution would form a closed system, which is based on the mutual confidence of the members."* Many central bankers would still no doubt be reluctant to go even thus far; but their "mutual confidence" within the community is stronger than their mutual confidence within a wider group such as IMF.

Moreover, the central bankers' unwillingness to pass powers over to a common institution, at least on the European scale, should gradually be softened by the slow erosion of their own effectiveness, which is already resulting from the freer movement of funds across national frontiers. "We shall fairly soon reach a point," M. Bertrand says, "when national money markets will no longer be under the control of national governments . . . centralisation of credit control will be essential in order to give effectiveness and coherence to an instrument of policy which, at the national level, is bound to become progressively weaker."

Quick results, it must be repeated, can hardly be expected from this European front; all that can be said is that Europe's financial authorities are likely to be a little less conservative about setting up a credit creating institution for the common market in Paris than about a credit creating institution for the world in Washington. What Mr. Maudling must now ensure is that Britain's weight is thrown behind the progressive, integrationist school wholeheartedly, and not only at those selected points at which there is a clear short-term advantage for sterling. M. Bertrand, from his close range view, has some damning things to say:

> Paradoxically, there is a fairly widespread feeling on this side of the Channel that British entry into the common market may check the movement towards monetary integration. This idea is based on observation of the tendencies of British international monetary policy over the last few years, which have been eminently

* Aspects of European Integration, page 138. PEP, 16, Queen Anne's Gate, SW1. 15s.

conservative. Britain had reservations about the European Payments Union, and later about the European Monetary Agreement, but was in favour of bilateral arrangements such as the Basle operation; it would certainly have preferred the special reserves of the Monetary Fund to be purely and simply an extension of the quota system.

Mr. Maudling's initiative has gone some way to redress the balance. Its poor reception in Washington, among American and European officials alike, should not swing him back now to the old road of ad hoc expedients, which is easier to follow but leads nowhere. The integrationist path is not without followers in the common market, and it provides the only long run solution for Britain's international monetary problem.