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British and American Plans for International Currency Stabilization

THE BRITISH PLAN of Lord Keynes for an International Clearing Union and the United States Treasury plan for an International Stabilization Fund (known as the White plan), both of which were originally announced in April 1943, are efforts toward greater international cooperation in monetary matters. They are evidence that exchange stability is considered a major postwar problem. Both are tentative proposals offered by technical experts as a basis for study and discussion.[1] On the basis of discussions with experts of the various countries, the U. S. Treasury Department released a revised draft of its proposal on August 20, 1943, which is still considered tentative; the revised draft has been used in this study.

This analysis presents a brief comparison of the main features of the two plans, and a short commentary intended to make clear some of the difficulties that may be encountered in applying them. Another section treats the obstacles that may beset any general stabilization plan inaugurated now or in the immediate postwar period, and the financial effects that such plans may be expected to produce. The final section considers an alternative method of treating the problem, the key-country approach.

[1] Canadian experts, after studying the Keynes and White plans, prepared tentative draft proposals for an International Exchange Union, which were made public in July 1943 by the Canadian Minister of Finance, the Hon. J. L. Ilsley. This Canadian plan embodies important features of both the Keynes and White plans, but has greater similarity to the White plan. It provides for an International Exchange Union with a capital fund of $8 billion, and, in addition, member countries could be required to make loans to the Union in amounts up to 50 percent of their quotas. In its concepts, techniques, and general powers, however, it is very similar to the White plan. For that reason it has not been thought necessary to include in this study an analysis of the Canadian plan.

FEATURES OF THE PLANS

Each plan provides a mechanism for granting foreign credits to member countries and for trying to promote conditions under which payments between countries arising out of international transactions may tend to be brought into balance and maintained in a state of equilibrium. The term "Clearing Union" is not an accurate description of the agency proposed by Keynes because it is essentially a credit mechanism rather than a clearing mechanism.

Each plan provides for a new international monetary unit which would be used for tying the various currencies to gold and to each other. The new unit would be used for accounting purposes but not for circulation. In the Keynes plan, the unit of account is called "bancor"; in the White plan, it is called "unitas." Each would have a definite relationship with gold and with the currency of each member state. Hence, each plan involves a definite relationship between the currencies of the various countries and gold.

Both plans contemplate the use of gold in settling international balances, and both provide an unlimited market for gold at the established price. Member countries may buy and sell gold freely at the fixed value, but the White plan seems to place the greater emphasis on the importance of gold as an international standard of value. The gold value of unitas could be changed only with the approval of 85 percent of the member votes; that of bancor presumably could be changed by majority vote. The Keynes plan does not favor full two-way convertibility, and suggests that if member countries should prefer to maintain full convertibility for internal purposes, they might permit the export of gold only under license as a protective measure.

The adherence of the White plan to gold, and its objective of stabilizing currencies in relation to gold, implies that the dollar price of gold will not again be manipulated to influence domestic commodity prices.

In each plan the international agency would deal only with the central banks, treasuries or fiscal agents of the member countries, and, according to their sponsors, would not interfere with the existing agencies or methods of financing international transactions. Central banks or treasuries would keep accounts with the International Clearing Union or Stabilization Fund, in terms of bancor or unitas as the case might be, and would use the central agency for dealing with exchange balances between countries.

The process of granting credits differs somewhat in the two plans. The Clearing Union of the Keynes plan, having no funds to begin with, would provide overdraft facilities to member countries. For example, if country A ~~has a debit~~ balance with country B, the Clearing Union would debit A and credit B. A country having a favorable balance of payments with the rest of the world as a whole would find itself building up a credit account with the Clearing Union in terms of bancor. In other words, the creditor countries as a group would, in effect, be extending credits to the debtor countries as a group.

The importer in the debtor country would deposit funds with his bank as usual for goods received and, if exchange were not available in the exporter's country, the importer's bank would deposit the funds in its own central bank. The central bank would simply credit the Clearing Union. The exporter in the creditor country would receive pay from his bank as usual for goods shipped. His bank would be reimbursed by the central bank of that country and the latter would debit the Clearing Union. The net result would be that the country with excess payments would develop a debit balance with the Union and the country with excess receipts would develop a credit balance with the Union.

The Stabilization Fund of the White plan, having assets to begin with, would exchange one currency for another or buy one currency and sell another. The Fund would also have means of increasing its supply of any currency, i.e., by borrowing or by selling some of its assets. In both plans measures are contemplated that would limit the amount of credit extended to any country.

SIMILARITY OF OBJECTIVES

The objectives of the two plans are similar. They would attempt immediate over-all stabilization of foreign exchange rates and try to promote conditions under which stability can be maintained. They would seek to reduce foreign exchange controls that interfere with world trade, and would help to eliminate bilateral exchange clearings, multiple currency devices, blocked balances, and discriminating foreign exchange practices. In general the aim would be to promote and maintain equilibrium in international transactions.

After the last war efforts to stabilize currencies were sporadic and uncoordinated; some countries undervalued and some overvalued. Instances occurred when the decision of one country to change the value of its currency caused others to follow suit. One country's difficulties led to the imposition of various exchange controls and trade restrictions. These in turn sometimes led to retaliatory measures by other countries, and variations in exchange rates were used as measures of economic warfare.

These monetary difficulties were in part the result of a lack of general economic cooperation among the countries of the world. Tariff barriers and other trade restrictions added to the monetary troubles, and monetary troubles in turn increased trade difficulties, retarding the establishment of balanced international economic relations. Disequilibria were obscured for a period by the flow of capital, much of it short-term, from creditor to debtor nations, but the borrowing nations were building up economies that could continue only on the basis of a constant inflow of new loans. This increased the ultimate strain on the international monetary organization.

International economic relations may be even more difficult to adjust after the present war, and the problem that concerns governments today is how to prevent the same kind of chaos that prevailed in the world's monetary and trade relationships during much of the 1920's and 1930's. This war has been far more destructive than the previous one and has created greater dislocations, both in international economic relations and in the internal economies of many countries—especially the Continental European countries.

The proposed credit agencies are not designed to finance relief and reconstruction, and the sponsors of the plans recognize the need for other agencies to provide funds for these activities. The feasibility of making a distinction in actual operations, however, is doubtful. The stabilization agency would finance passive balances, and the passive balance of a country would be due to the fact that it needs, or buys, the world's goods in excess of its ability to export. The establishment of other agencies to supply the needs for relief and reconstruction would ease the burden on the stabilization agency but might not relieve it entirely from supplying such needs.

There are still important differences in details between the two plans, but discussions are continuing in an effort to remove such differences and to determine the nature of the difficulties involved in any over-all stabilization plan.

MEMBERSHIP AND ADDITIONS TO MEMBERSHIP[2]

WHITE PLAN—*An International Stabilization Fund will be established in which all the United Nations and those nations associated with them in this war will participate.*

KEYNES PLAN—*All the United Nations will be invited to become original members of the International Clearing Union. Other states may be invited to join subsequently. If ex-enemy states are invited to join, special conditions may be applied to them.*

Postwar help in rehabilitating the ex-enemy countries and in aiding the stabilization of their exchanges is partly a political question. Some aid to ex-enemy countries may be required, however, if we are to attain the desired economic order in the world. The greatest need for stabilization aid will probably be felt by the ex-enemy countries, by the eastern and southeastern European countries, and perhaps by China. South American countries as well as a few of the European countries may have enough gold and foreign

[2] In the following comparisons of the technical features of the two plans, the wording frequently follows closely that used in the documents themselves.

exchange to tide them over the initial stabilization period without large credits, although some of them may need relief aid and long-term reconstruction loans.

QUOTAS OF MEMBER COUNTRIES

WHITE PLAN—*This plan sets up a Fund of at least $5 billion consisting of currencies and securities of member governments and of gold. Each country would subscribe a specific quota to this Fund, the quotas to be determined by some agreed-upon formula which takes into consideration such factors as holdings of gold and free foreign exchanges, magnitude and fluctuations in balances of international payments, and national income. On or before the date set for the Fund's operations to begin, each country would meet its quota contribution in full, partly in gold and partly in local currencies and securities. Any changes in the formula by which the quotas are determined would require a four-fifths vote of the Board. Quotas would be adjusted on the basis of the most recent data three years after the establishment of the Fund and at five-year intervals thereafter in accordance with the agreed-upon formula but any increase of a quota must be approved by the representative of the country concerned. Where a quota is clearly inequitable it may be increased during the period between adjustment dates.*

KEYNES PLAN—*No provision is made under this plan for a fund or stated assets at the time of organization. It merely sets up a Clearing Union that would establish overdraft facilities for member countries. The Union would settle balances between countries simply by debiting one and crediting the other. The extent of these transactions would be regulated by the quotas assigned to each member country. The initial quotas might be fixed by reference to the sum of each country's exports and imports on the average of (say) the three prewar years, and might be (say) 75 percent of this amount. It is a matter for discussion whether the formula should take into account other factors. After the lapse of the transition period quotas would be revised annually.*

One important difference between the two plans is the determination of quotas for member countries, i.e., the extent of their participation. Quotas are used not only as a basis for determining rights to credit facilities, but also as a measure of voting power.

The sum of the quotas under the White plan would be fixed at a minimum of $5 billion. If all but ex-enemy countries should join the Clearing Union, the sum of the quotas under the Keynes plan, however, would aggregate about $30 billion on the basis of 1936-38 trade figures. The United Kingdom would have about 16 percent of the total, the British Empire about 35 percent, and the United States about 14 percent. If fewer countries should join, the total of all quotas would be less, and each member country would have a larger proportion of the total.

Under the Keynes plan foreign countries could in theory accumulate debits of nearly $26 billion. That is a theoretical limit based on the assumption that the United States would be the only creditor country[3] and all others would be debtor countries, and further that none of the safeguards provided for worked. That would not occur, of course, but it might be possible after a period of years for debit balances to reach half that figure, or even more, if creditor countries should continue to supply the funds without making any use of their credit balances.

In the case of the White plan, a country's quota represents the amount which that country is obligated to bear in financing the plan. If the United States' quota should be $2 billion, for example, that is the extent to which the United States is obligated to contribute. The United States, however, could contribute more by lending additional dollars to the Fund or by making other special arrangements to supply dollars. In the Keynes plan, on the other hand, a country's share in the financing would depend on the size of the credit balance it accumulates, which could conceivably equal the sum of the debit balances of all other member countries.

The borrowing facilities provided under the Keynes plan seem unusually large to be used merely for short-term stabilization credits. The size of the quotas raises the question as to whether the borrowing facilities might not be used for other purposes.

DETERMINATION OF RATES OF EXCHANGE

WHITE PLAN—*Initial rates of exchange shall be based upon the value of the currency in terms of United States dollars which prevailed on July 1, 1943, or if that should be inappropriate, the rate would be determined by consultation between the member country and the Fund. For a member country which has been occupied by the enemy, the rate would be fixed by the liberated country in consultation with the Fund and at a level acceptable to the Fund. The Fund shall determine the range within which the rates may fluctuate.*

After an initial period, changes in rates could be made only with the approval of three-fourths of the member votes including the representative of the country concerned. During the first three years of the Fund's operation, however, changes may be made with the approval of a majority of member votes, and a member country may change the rate for its currency by as much as 10 percent without the approval of the Fund, provided it shall notify the Fund of its intention and consult with the Fund on the advisability of the action.

KEYNES PLAN—*This plan contemplates that some general agreement will be reached between the member countries regarding the relative values of the different currencies before the plan goes into effect. No indication is given as to the methods that might be used to determine the initial rates or the factors that should be taken into consideration.*

Changes in rates could not be made without the permission of the Governing Board of the Clearing Union, except that a member country could change its rate

[3] "Creditor country," as used in this report, means a country with a favorable balance of payments, and "debtor country" means a country with an unfavorable balance of payments.

once as much as 5 percent without the approval of the Board, provided its debit balance has exceeded a quarter of its quota on the average of at least two years.[4]

The attempt to stabilize rates for all countries immediately after the war before general political and economic stability has been restored and to support these rates by credit would encounter serious obstacles. It might not be easy to obtain the necessary votes for a change and action by the Fund (or Union) might lag behind activities in the exchange market. Political bargaining might delay needed actions. The problem of immediate over-all stabilization is reserved for general comment at the end of this analysis.

MANAGEMENT AND CONTROL

WHITE PLAN—*Each country shall have a representative on the Board of Directors, which shall meet annually. The Board would appoint a Managing Director and also an Executive Committee of not less than eleven members which would be continuously available at the head office of the Fund to exercise the authority delegated by the Board. It is suggested that each country might have 100 votes plus one vote for each 100,000 unitas ($1 million) of its quota, except on questions of the sale of foreign exchange and membership. No country, however, may cast more than one-fifth of the total votes. In general, a majority vote would govern except on certain specified questions where a vote of 75, 80 or 85 percent would be required.*

KEYNES PLAN—*The Keynes plan provides for a Governing Board not to exceed (say) twelve to fifteen members. The states with the larger quotas would have individual representation on the Board but the states with the smaller quotas might be arranged into convenient political or geographical groups, each group appointing a representative. Member states not individually represented on the Board might appoint permanent delegates to the Union to maintain contacts and act as liaison. Each representative on the Governing Board would have votes in proportion to the quota of the state or states appointing him, except on a proposal to increase a particular quota in which case there would be a modification of the voting power.*

Under the White plan no country would have more than 20 percent of the votes. Under the Keynes formula for quotas, assuming all but ex-enemy countries would join the Union, the United Kingdom would have 16 percent of the votes, the British Empire 35 percent, and the United States 14 percent, as shown above.

The voice that each country will have in the management will probably be one of the difficult points of agreement. The United States, as the largest

[4] Keynes, however, allows a five-year period in which appeals for changes in exchange rates shall be given special consideration if made on the grounds of unforeseen circumstances. In addition he points out in his article, "The Objective of International Price Stability," *The Economic Journal,* London, June-September 1943, pp. 185-87, that changes in exchange rates which become necessary as a consequence of varying price policies in the member countries, are to be made whenever the contingency arises. Only changes in exchange rates consequent to shortages in means of foreign payments are to be avoided.

creditor country, will make the greatest contribution, whatever plan may be adopted, and probably will expect to have a substantial voice in the management. On the other hand, the smaller countries, many of whom would make genuine contributions to the success of the scheme, will be exceptionally sensitive to anything that smacks of domination by any one power, or any two powers, for that matter. Political considerations will doubtless play a part in the decisions regarding control, especially where the plan must be approved by legislative bodies. It might be preferable, therefore, to divorce the technical problem of the size of the quotas from the political problem of control.

GENERAL POWERS

WHITE PLAN—*The International Stabilization Fund shall have the following powers:*

a. To buy, sell, and hold gold, currencies, and government securities of member countries; to transfer and earmark gold; to issue its own obligations and discount or offer them for sale in member countries.

b. To sell to any member country the currency of any member country which the Fund holds, provided that the foreign exchange is required to meet an adverse balance of payments predominantly on current account with the country whose currency is being demanded. (There are definite limitations on the Fund's holdings of the currency of any member country, but this will be covered in a later section.) Under prescribed conditions the Fund may also sell foreign exchange to a member country to facilitate the transfer of capital, or the repayment or adjustment of foreign debts.

c. To buy and sell currencies of non-member countries under certain conditions; to borrow the currency of any member country; to sell member country obligations owned by the Fund, provided the representatives of the country issuing the obligation as well as the country in which the securities are to be sold approve; to obtain rediscounts or advances from central banks; to invest its currency holdings in government securities of the country of that currency provided the representative of the country approves; to lend to any member country its local currency, within limitations; and to levy upon member countries a pro rata share of the expenses.

KEYNES PLAN—*The Clearing Union shall have power to set up the machinery for extending credits and clearing balances, to fix the value of bancor in terms of gold, to change the value of individual currencies in terms of bancor under certain conditions, to reduce or raise quotas, to reduce the quotas of all members in the same proportion if deemed necessary, to recommend and discuss with member states measures for correcting continuous debit or credit balances, and to ask member states for relevant statistical or other information.*

The Keynes plan provides for a lending mechanism without other broad banking powers, and, on the surface, seems the simpler plan, even though it provides more extensive credit facilities. The White plan endows the Stabilization Fund with powers to engage in a wide variety of international banking operations. It could lend and borrow money, and deal in securities. The fact that it could borrow money and issue its own obligations might bring the Fund's activities nearer the scope of the Keynes Union. In spite of its limited size some criticism has been directed at the Stabilization Fund because it would be able to carry on extensive activities. These general banking powers which the Fund would have, however, do not seem to be any more comprehensive than those now possessed by the Bank for International Settlements. The purpose of these powers is to enable the Fund to cooperate effectively with the monetary authorities of the member countries.

It has been suggested that an institution which can engage in these broad banking activities might compete with existing commercial banks and interfere with the regular channels of international trade and international banking. The plan provides, however, that the Fund shall deal only with or through treasuries and central banks. Therefore, the Fund could not engage in general banking activities except with the consent of the member countries involved; instead, it would use its powers to cooperate with the local monetary authorities. Mr. Morgenthau said of the Stabilization Fund, when it was originally announced: "It would not compete with private banks or existing agencies. Its operations would be maintained only to supplement the efforts made by each member government to maintain monetary stability. The established channels of international trade and international banking would be retained in full for all international transactions."

This contention would probably be true so far as it relates to the financing of specific international transactions. In a broader sense, however, such a method of extending credits to settle international balances might reduce the amount of credits that would otherwise be extended through existing facilities.

Some interference with existing agencies and practices might also seem to be implied in the provision that each member country shall agree to offer to the Fund one-half of its additional acquisitions of free and liquid foreign exchange and gold in excess of its holdings at the time it became a member, and to discourage the unnecessary accumulation of foreign balances by its nationals. The purpose of that provision, however, is to safeguard the Fund against the misuse of its resources by a member country. With that provision a country could not continue to buy foreign exchange from the Fund while at the same time accumulating excessive holdings of gold and foreign exchange independently. No country would be under obligation to sell gold and foreign exchange to the Fund except for its local currency or foreign currencies acceptable to it. A creditor country, of whose currency the Fund has only a small or moderate amount, would not sell additional accumulations of gold and foreign exchange to the Fund because the Fund would not have the local currency to pay for such purchases.

The Fund is also given power to deal in securities and to make loans, but it is doubtful whether these operations would compete with existing banking institutions. The purpose of these powers seems to be to permit countries without adequate money markets and with rigid monetary systems to offset any expansionist or contractionist effect that their dealings with the Fund might otherwise have. Such activities can be undertaken only with the approval of the member country.

Concerning his plan, Keynes states: "No transaction in bancor will take place except when a member State or its Central Bank is exercising the right to pay in it.... Thus the fabric of international banking organisation, built up by long experience to satisfy practical needs, would be left as undisturbed as possible."

THE PROBLEM OF DEBIT BALANCES

WHITE PLAN—*The Fund's holdings of the currency and securities of any member country shall not exceed that country's quota by more than 50 percent during the first year of operation, or by more than 100 percent thereafter except as otherwise provided. The total holdings thus permitted are termed* permissible quota. *With the specific approval of the Board the permissible quota may be exceeded provided at least one of the following conditions is met:*

a. In the judgment of the Fund satisfactory measures are being or will be taken by the country whose currency is being acquired to correct the disequilibrium in the country's balance of payments, or

b. It is believed that the excess accumulation will be temporary.

It is further provided that when the Fund's holdings of any member country's currency fall below 20 percent of the country's quota, the sale of such currency shall require approval of the country's representative.

When the Fund's holdings of any local currency and securities exceed the permissible quota, that country may be required to deposit collateral with the Fund. When a member country, whose currency and securities held by the Fund exceed its quota, is exhausting its permissible quota more rapidly than seems warranted, or is using its permissible quota in a manner that clearly has the effect of preventing or unduly delaying the establishment of a sound balance in its international accounts, the Fund may place such conditions upon additional sales of foreign exchange to that country as it deems to be in the general interest of the Fund. A charge of not less than 1 percent per annum payable in gold may be levied against any member country on the amount of its currency held by the Fund in excess of the quota of that country. An additional charge, also payable in gold, shall be levied against holdings of a member's currency in excess of the permissible *quota. A country whose debit balance exceeds the quota, however, may repurchase the excess by paying to the Fund gold or acceptable foreign exchange. As pointed out above, each member country agrees that it will offer to sell to the Fund, for its local currency or for foreign exchange which it needs, one-half of the gold and foreign exchange it acquires in excess of its official holdings at the time it became a member of the Fund.*

Keynes Plan—*A member state may not increase its debit balance by more than a quarter of its quota within a year without permission of the Governing Board. If its debit balance has exceeded one-fourth of its quota on the average of at least two years, it may reduce the value of its currency in terms of bancor without the consent of the Governing Board, provided the reduction shall not exceed 5 percent. But this procedure cannot be repeated without the approval of the Board.*

The Governing Board may require a member state having a debit balance equal to half its quota to deposit suitable collateral. As a condition of allowing a member state to increase its debit balance to more than half its quota, the Board may require all or any of the following measures:

a. A reduction in the value of the member's currency,

b. The control of outward capital transactions, and

c. The surrender of a suitable proportion of any separate gold or other liquid reserve it may have in reduction of its debit balance.

Furthermore, the Governing Board may recommend to the member state any internal measures affecting its domestic economy that may appear appropriate to restore the equilibrium of its international balance.

If a member state's debit balance has exceeded three-fourths of its quota on the average of at least a year and is excessive in the opinion of the Governing Board, or is increasing at an excessive rate in relation to the total debit balances outstanding on the books, it may be asked to take measures to improve its position. In the event of its failing to reduce its debit balance within two years, the Board may declare it in default and no longer entitled to draw against its account except with permission.

A member state shall pay 1 percent per annum on the amount of its average bancor balance which is in excess of one-fourth of its quota, whether it is a debit or a credit balance; and a further charge of 1 percent on its average balance in excess of one-half of its quota, whether credit or debit. Thus only a country which keeps in a state of approximate international balance on the average of a year will escape this contribution.

The matter of dealing with debit balances would be the major problem of any international agency set up to stabilize exchanges. It is here that the mechanism would succeed or break down. Both institutions are postwar lending agencies designed to give debtor countries time to make their adjustments and bring their payments into balance. Presumably the efforts of the stabilization agency would be supplemented by programs for relief and reconstruction loans. To prevent the agency from being utilized for those purposes would be difficult, however, because whatever would increase the passive balance of payments would create a demand on the agency. Therefore, there is little likelihood that its operations would be limited to supplying short-term credits. Political and economic stability, moreover, go hand in hand with exchange stability and there are many basic causes of disequilibrium which may not be cured by loans and credits.

One striking feature of both plans is that no tests or standards are set up for debtor countries in making initial credits. An open line of credit is made available to all member countries without imposing upon them any initial requirements, except the general obligations assumed when they become members. The White plan does provide that after a member country has borrowed from the Fund an amount in excess of its gold contribution to the Fund, the Fund may place conditions upon additional sales of foreign exchange to that country. The author of the plan apparently has much faith in the protective value of that provision. However, it would be very difficult at that stage of operations for the Fund to refuse credit to a country that had just become a member in the belief that it had a line of credit equal to its defined permissible quota. It would not be easy to determine when such a country was exhausting its permissible quota too fast or to appraise the probable effectiveness of its efforts to put its house in order. The tendency might be for the Fund to be too generous rather than too strict.

Both plans assume that member states will act in good faith and that they will undertake whatever internal measures may be necessary to maintain equilibrium in their international payments. Whether this would be a sufficient safeguard to make it a sound system of credits is questionable. The creditworthiness of member countries would vary greatly and it would be difficult to prevent some of them from taking advantage of a line of credit. This might be especially true under the Keynes plan because of the large credit facilities provided.

The White plan is not very specific as to what measures the Board of Directors may take to induce the correction of excessive debit balances. It simply says that certain limits may be exceeded if in the judgment of the Fund satisfactory measures are being or will be taken by the country to correct disequilibrium in the balance of payments. The Keynes plan says that the Board may require a reduction in the value of a member's currency or the control of capital exports or the surrender of gold and other reserves. A central board with a capable technical staff will presumably be in a position to diagnose the exchange troubles of any debtor country and to recommend corrective measures.

Whether the causes of the difficulties can be remedied within a reasonable time depends on how deep-seated they may be or how much effort member countries may exert in that direction. A lack of balance is not always a temporary matter. The trend of payments may run consistently in one direction, and the granting of credits may simply postpone the necessity for taking corrective measures. The member countries make only general commitments to take corrective measures, and if the need calls for strenuous action they may hesitate and delay. The size and variability of the debit balances would be the test of the success of the plan, and would determine whether the credits extended are really capital (long-term) loans.

CONTROL OVER SHORT-TERM CAPITAL MOVEMENTS

WHITE PLAN—*Member countries agree to cooperate in regulating capital movements in various ways, including:*

a. The refusal to accept deposits, securities or investments from the nationals of any member country imposing restrictions on capital exports except on permission of that country and the Fund; and

b. The furnishing of full information on property in the form of deposits, securities and investments held in their respective jurisdictions by the nationals of a country restricting capital exports.

KEYNES PLAN—*As a condition of allowing a member state to increase its debit balance to more than half its quota, the Board may require, among other measures, the control of outward capital transactions, as pointed out previously.*

Keynes says that it is widely held that the control of capital movements, both inward and outward, should be a permanent feature of the postwar system. But he holds that such control cannot be regarded as essential to the operation of the Clearing Union, and therefore proposes that it should be left to the decision of each member state. It would be of great advantage, he declares, if the United States and other members of the Union would adopt machinery similar to that of the British Exchange Control, so that records of international movements of funds would be available.

While both plans contemplate control over international movements of capital, this control would be exercised by the member countries themselves with the approval of the Stabilization Fund or Clearing Union. This applies largely, of course, to the flight of funds for political reasons or to evade domestic taxation, or to any outflow of funds from debtor countries that lack the means to finance such capital exports. Medium- and long-term loans by creditor countries that will help to maintain equilibrium and develop the world's resources will be encouraged, presumably by setting up an international investment organization.

The question arises here as to whether capital movements can be regulated without control of practically all exchange transactions. There are so many ways by which capital may be transferred that it is sometimes exceedingly hard to discriminate between current account and capital account. What may seem to be simple current transactions may turn out to be capital transfers. Goods may be bought in one country and sold in another, thereby effecting a transfer of capital. The nationals of a country which had built up a heavy debit balance with the central stabilization agency might ship goods to the United States and invest the proceeds here instead of reducing the debit balance by turning over the dollars to the central agency. If exchange stabilization should turn out to depend upon control of capital movements, it might require the policing of all transactions. Hence, these plans might extend and perpetuate exchange controls instead of removing them.

Keynes says: "There is no country which can, in future, safely allow the flight of funds for political reasons or to evade domestic taxation or in anticipation of the owner turning refugee. Equally, there is no country that can safely receive fugitive funds, which constitute an unwanted import of capital, yet cannot safely be used for fixed investment." This is a strong note of nationalism and is reflected in both international plans. If, as Keynes thinks, the postwar world will continue to have refugees and flights of capital for political reasons, conditions will scarcely be favorable for an over-all stabilization scheme.[5] Political stability has always been a *sine qua non* of exchange stability.

THE PROBLEM OF CREDIT BALANCES

WHITE PLAN—*When the Fund's holdings of the currency and securities of a member country become excessively small in relation to prospective acquisitions and needs for that currency, the Fund will render to the country a report embodying an analysis of the causes of the depletion of its holdings of that currency, a forecast of the prospective balance of payments, and recommendations for increasing the Fund's holdings of that currency. This report would be sent to all member countries and, if deemed desirable, made public.*

When it becomes evident to the Board of Directors that the Fund's holdings of a particular currency will not be sufficient to meet all demands, steps will be taken to see that the distribution is equitable. Furthermore, the Fund will make every effort to increase the supply of the scarce currency.

The Fund has various ways of increasing its holdings of member country currencies. Perhaps the most important method is the power to borrow from central banks, with the approval of the member countries concerned. The Fund may also issue its own obligations and discount or offer them for sale in member countries. Also "the Fund may make special arrangements with any member country for the purpose of providing an emergency supply under appropriate conditions which are acceptable to both the Fund and the member country." Thus, while there is a definite limit to the original contribution, the United States and other creditor countries might be asked to extend voluntarily additional amounts in order to keep the plan operating.

KEYNES PLAN—*A member state whose credit balance has exceeded half its quota on the average of at least a year shall discuss with the Governing Board (but shall retain the ultimate decision in its own hands) what measures would be appropriate to restore the equilibrium of its international balances, including:*

a. Measures for the expansion of domestic credit and domestic demand,
b. The appreciation of its local currency in terms of bancor, or, alternatively, the encouragement of an increase in money rates of earnings,
c. The reduction of tariffs and other discouragements against imports, and
d. International development loans.

A member state may obtain a credit balance in bancor by depositing gold with

[5] Imre de Vegh contends that: "A perpetuation and legalization of control over capital movements is not compatible with any notion of a world that supposedly combats violence and dictatorial forms of government." ("The International Clearing Union," *The American Economic Review*, September 1943, p. 539.)

the Clearing Union, but no one is entitled to demand gold from the Union. The Governing Board, however, may at its discretion distribute any gold in its possession to members possessing credit balances in excess of a specified proportion of their quotas.

As previously stated, a member state would also be required to pay interest on its credit balance above a certain amount.

Both plans recognize the responsibility of creditor countries to help correct the disequilibrium in the exchanges. In case of credit balances, of course, no rigid maxima are proposed, nor do they deprive any member state of any of the facilities that it now possesses for receiving payment for its exports. A creditor country may continue to employ the proceeds of its exports to buy goods or investments abroad, to buy gold, or to make temporary advances. Creditor countries may be asked to adopt credit policies or trade and tariff policies that will help to cure the disequilibrium, but there is no force to compel the acceptance of such suggestions. The penalty would be the continued accumulation of credit balances. We have noted in a previous section how much greater a country's obligation to extend credits might be under the Keynes plan than under the White plan.

The provision in the Keynes plan that the lending countries should pay interest on their credit balances above a certain amount is most unusual. The purpose is to induce creditor countries to take the steps necessary to reduce their credit balances, but it is difficult to imagine the United States or any other prospective creditor country agreeing to such a provision. It appears to be a proposal to penalize a creditor country in order to induce it to accept means of settlement that it would otherwise be unwilling to accept.

Probably the United States will have a big favorable trade balance for several years after the war. The rest of the world will need our goods, and their problem will be to get dollars to pay for them. Not only would the United States be the principal supplier of credits, but to make either plan successful we would also have to supplement our credits with long-term loans.

We shall probably also continue to draw gold into the United States. Many countries may use gold to buy dollars without going through the clearing agency, since both plans contemplate the free use of gold in settling international balances. In addition, gold might flow to the United States from the Stabilization Fund, because much of the gold deposited with the Fund by the various countries might be used to buy dollars.

EFFECT ON MONEY MARKETS

The Keynes plan seems to place much more emphasis on the management of money markets as a means of aiding stabilization than does the White plan. To remedy excessive credit balances, for example, Keynes advocates measures of expansion of domestic credit and domestic demand as well as steps to appreciate local currencies or increase money rates of earnings. In countries developing excessive debit balances, he would reduce the value of a member's currency, in terms of gold and other currencies, as an anti-deflationary measure. In other words, the Keynes plan would involve a large degree of monetary management within each member nation by its government, although in case of the creditor countries the ultimate decision would be left to the country itself.

The operation of either plan, without monetary management, could affect money markets very much as the importation and exportation of gold did under the old gold standard; that is, the operations could be contractionary in debtor countries and expansionary in creditor countries.[6] Whether either plan would actually work out that way, of course, would depend upon whether the debtor and creditor countries proceed to offset the effects of the operations of the plan on their money markets. If the creditor countries should permit the expansionist effects and the debtor countries should offset the contractionist effects, the general effect on the world would be expansionist.

In the debtor country, the accumulation of local currency in the central bank would tend to reduce the reserves of the commercial banks and have a contractionist influence. This, according to standard monetary theory, would tend over the long run to reduce prices in comparison with those in other countries, encourage exports and discourage imports. If the debtor country, however, should choose to offset this influence by central bank open-market operations or other monetary activities, it could avoid contractionist pressure. This, of course, might increase the time necessary to bring about conditions of stability.

In the case of the creditor country, the purchase of foreign exchange from the market by the central bank would increase commercial bank reserves,

[6] John H. Williams has pointed out that the monetary mechanism provided in both plans is essentially a gold standard mechanism. ("Currency Stabilization: The Keynes and White Plans," *Foreign Affairs*, July 1943, p. 648.)

A somewhat different viewpoint is presented by Joan Robinson who says: "Both schemes are an improvement, from the point of view of deficit countries, not only on the gold standard, but also on a regime of free exchanges. The gold standard imposes severe deflationary pressure on a deficit country and forces it to redress its balance in the most disagreeable and wasteful manner. Each scheme provides alternative and less painful methods of redress. . . . What is required is a system in which deficit countries can depreciate to establish equilibrium, while surplus countries are prevented from indulging in 'exchange dumping' merely to increase their surpluses. A scheme of international control of exchange rates, provided that it is genuinely international and is not manipulated in favour of particular interests, promises great advantages to deficit countries, which would be well worth the sacrifice of national autonomy which it involves." ("The International Currency Proposals," *The Economic Journal*, June-September 1943, pp. 171-72.)

thereby producing an expansionist tendency; prices might tend to rise, which would encourage imports and discourage exports. Here again, a country could offset this influence just as it can offset the effect of gold imports.

Under the Keynes plan the United States would finance debtor countries with Federal Reserve Bank credit to the extent of our credit balance, and the possible extent of that credit balance as shown in a previous section indicates what a burden this financing might become. The banks and dealers in foreign exchange would sell their surplus holdings of foreign exchange to the Federal Reserve Banks and the latter would in turn receive a credit balance in bancor. To the extent of our credit balance, therefore, operations under the Clearing Union would be just as expansionist as if we imported gold for the same amount, because they would increase member bank reserves. But this expansionist tendency would not be limited by the amount of available gold; it would be an addition to the influence of gold imports. The effects could be offset, of course, if the Federal Reserve authorities had sufficient securities to sell in the open market or sufficient powers to raise reserve requirements. Regardless of the ability of the Federal Reserve System to offset expansionist effects, the suggestion for financing the balance of payments through central bank credit should receive critical examination to determine its various implications. The time might come when the assets behind our own Federal Reserve notes and behind member bank reserves would consist in some part of bancor which in turn would be backed by a miscellaneous assortment of weak currencies.

The White plan would have a similar expansionist effect to the extent that the Stabilization Fund should borrow from the Federal Reserve Banks. Such borrowing might be substantial, since that apparently would be the principal means for the Fund to acquire additional dollars after the original contribution of dollars and gold becomes exhausted.

It may be, however, that many countries would continue to manage their money markets with a view to domestic policies rather than for the purpose of curing debit or credit balances, especially if there should be a conflict between domestic policy and international policy. Some countries may be committed to high employment or to specific social policies, even if it means unbalanced budgets. Others may feel committed to stable interest rates for many years because of the conditions created by war financing. It is a question, therefore, to what extent they would permit the operation of an international stabilization mechanism to interfere with these internal policies.

LIMITATIONS ON ACTIONS OF MEMBER COUNTRIES

WHITE PLAN—*In addition to agreements by the member countries to cooperate in carrying out the plan, to adopt appropriate legislation, to furnish information to* *the Fund, and to give consideration to the views and recommendations of the Fund, there are some specific limitations imposed upon the actions of each country, such as agreement:*

a. Not to alter exchange rates without the consent of the Fund, except within the 10 percent limit permitted;

b. Not to undertake exchange dealings with other countries that would undermine stability of exchange rates established by the Fund;

c. To abandon as soon as conditions permit all restrictions over foreign exchange transactions with other member countries (except on capital transfers) and not to impose additional restrictions (except on capital transfers) without the consent of the Fund;

d. Not to enter upon any new bilateral clearing arrangements, or to engage in multiple currency practices, except with the approval of the Fund; and

e. To cooperate effectively with other member countries which adopt or continue controls over international capital movements.

KEYNES PLAN—*While the limitations imposed upon member countries by the Keynes plan are not always stated as specifically as in the White plan, they are clearly implied and quite similar. For example, a member state may not alter the value of its currency in terms of bancor without the permission of the Governing Board, except under certain stated conditions, and may not purchase or acquire gold at a price in excess of the price fixed by the Governing Board. Member states also agree to refrain from certain restrictive measures, such as import regulations and higher import duties, except under certain conditions.*

Keynes suggests that the Clearing Union might become the instrument and the support of international policies in addition to those which it is its primary purpose to promote. He suggests that the Union might become the pivot of the future economic government of the world. "There are various methods," he says, "by which the Clearing Union could use its influence and its powers to maintain stability of prices and to control the Trade Cycle. If an International Economic Board is established, this Board and the Clearing Union might be expected to work in close collaboration to their mutual advantage. If an International Investment or Development Corporation is also set up together with a scheme of Commodity Controls for the control of stocks of the staple primary products, we might come to possess in these three Institutions a powerful means of combating the evils of the Trade Cycle, by exercising contractionist or expansionist influence on the system as a whole or on particular sections."

Adherence to either plan calls for some suspension of sovereign rights; for example, the right to alter exchange rates, or the right to impose new exchange restrictions without the consent of the central agency, or the right to follow credit and financial policies disadvantageous to other countries. Any international organization or association involves the giving up or suspension of some freedom of action by the individual countries. The organizations proposed here, however, are not endowed with irrevocable powers because these powers can always be changed by vote of the member nations. Furthermore, a member country always has the option of withdrawing, although there might be some adverse effects on the country withdrawing, especially if it is a small country.

Besides these specific limitations on the powers of member countries, we have already noted that both plans either imply or would probably lead to rather broad international economic controls. The controls over capital movements, for example, in order to be successful and accomplish their purpose, might well involve controls over all international transactions. There is also implied in the plans, more specifically in the Keynes plan, substantial influence over the money markets of the individual countries. As a rule the control of money markets is left to the member countries themselves, but agreement to cooperate with the central agency and to take measures for promoting stability involves some degree of obligation to adopt such controls. But it is not always clear how far the powers of the central agency would go and how much pressure could be exerted on debtor countries.

WITHDRAWALS AND SUSPENSIONS

WHITE PLAN—*Any country may withdraw from the Fund by giving notice, and its withdrawal will take effect one year from the date of such notice.*

A country failing to meet its obligations to the Fund may be suspended by a majority of the member countries and at the end of one year the country shall be automatically dropped from membership unless it has been restored to good standing by a majority of the member countries. The rights of the Fund shall be fully safeguarded.

KEYNES PLAN—*Members may withdraw from the Union on a year's notice, subject to making satisfactory arrangement to discharge any debit balance. Similarly, the Governing Board may require the withdrawal of a member on the same notice if the latter is in breach of agreements relating to the Union.*

BLOCKED FOREIGN BALANCES

WHITE PLAN—*During the first two years, the Fund may buy from the governments of member countries blocked foreign balances held in other member countries, provided that the amount of the balances purchased does not exceed in the aggregate 10 percent of the quotas. At the end of two years the Fund shall propose a plan for the gradual further liquidation of blocked balances, and shall indicate the proportion of blocked balances that can be appropriately purchased under this provision.*

KEYNES PLAN—*The plan provides no detailed treatment for blocked balances, but its author suggests that special provision be made for converting blocked war balances into bancor.*

These blocked balances refer to balances blocked for lack of foreign exchange, such as the sterling balances now being accumulated in London by India and other countries. They do not include the balances blocked in the United States for political reasons.

Blocked sterling balances aggregate well over $4 billion now and are growing rapidly. A substantial proportion of these balances belongs to Empire countries, India being the largest holder. Some of them can probably be settled directly with the countries concerned, either by refunding or by the shipment of manufactured goods from England.[7] England will probably need substantial financial aid in dealing with blocked balances, but it is essentially a long-term operation and not a function of an exchange stabilization agency.

OTHER INTERNATIONAL FINANCIAL AGENCIES

WHITE PLAN—*In a memorandum attached to a letter inviting the ministers of finance of 37 countries to send technical experts to Washington to discuss suggestions for an International Stabilization Fund, the Secretary of the United States Treasury said in part: "It is recognized that an international stabilization fund is only one of the instrumentalities which may be needed in the field of international economic cooperation. Other agencies are also needed to provide capital for postwar reconstruction and development, to provide funds for rehabilitation and relief, and to promote stability in the prices of primary international commodities."*

The United States Treasury made public on October 8, 1943, an outline of a proposed plan for a United Nations Bank for Reconstruction and Development for the purpose of encouraging or providing long-term credits for the development of the productive resources of member countries. Its capital would be $10 billion, of which 20 percent would be paid in initially. Twenty percent of each payment would be made in gold.

The bank could guarantee loans made with private capital, participate in private capital loans, or make loans from its own resources when private loans are not available on reasonable terms.

The bank would deal only with or through governments of member countries, their central banks and fiscal agencies, and with or through international financial agencies that are owned predominantly by member governments. But with the approval of member countries the bank may guarantee international loans placed in their countries.

The board of directors would consist of one director, or alternate, appointed by each member government. The voting power of member countries would be closely related to their share holdings.

KEYNES PLAN—*In the preface to the Keynes plan, four main lines of approach to postwar problems are suggested:*

a. The mechanism of currency and exchange,

b. The framework of a commercial policy regulating conditions for exchange of goods, tariffs, and the like,

c. Orderly conduct of production, distribution, and prices of primary products, and

d. Investment aid, both medium- and long-term, for countries whose economic development needs assistance from outside.

The preface states further that while all these matters will need to be handled

[7] Cf. London *Economist*, August 7, 1943, pp. 180-81.

in due course, it appears convenient to give priority to the mechanism of currency and exchange.

As emphasized earlier, the sponsors of both plans contemplate that there will be other instrumentalities for promoting international economic cooperation and that these agencies will cooperate with and assist each other.

Stabilization plans of the kind proposed might have a better chance of success if coupled with other undertakings, especially with measures for handling relief and for making long-term reconstruction and development loans. The Treasury's plan for a world bank, as well as plans for postwar relief, will doubtless be considered along with plans for stabilization as parts of a general program of postwar financial reconstruction. The general feasibility of the plans, however, is the subject of the next section.

NOTE: Two French financial experts have also made public a plan for stabilizing exchanges. This plan proposes that the principal nations conclude a monetary accord, similar to the Tripartite Agreement, to which other United Nations would be invited to adhere. The official parities of the currencies of participating countries would be fixed and would not be changed without consultation or agreement. The stability of these exchange rates would be maintained by the monetary authorities of each country through the acquisition and holding of the exchange of other participating countries. Foreign exchange thus held could be utilized for payments to be made in such currencies. The amount of exchange a country's monetary authorities agree to acquire would be limited and each country would guarantee the holder against depreciation of its currency by the deposit, on demand, of collateral (gold, foreign bills, approved securities, raw materials, etc.) up to a specified percentage of the amount of such currency held by another participating country. As this virtual opening of mutual credits would involve inflationary risks, a method of sterilization is suggested to counteract this tendency whenever advisable. It is felt that the system would operate more smoothly if the monetary authorities of the participating countries were constantly in close contact, although an International Clearing Office is not considered an essential condition for the functioning of the plan. New York *Times,* May 9, 1943.