THE INTERNATIONAL MONETARY FUND 1945-1965

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VOLUME III: DOCUMENTS

Edited by
J. Keith Horsefield

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PREFATORY NOTE

This volume comprises documents relating to the history of the International Monetary Fund, including some which preceded the drafting of the Articles of Agreement. Among the latter are early versions of the plans for a Clearing Union (the Keynes Plan) and a Stabilization Fund (the White Plan) which have not hitherto been published.

The published documents of the Fund here reproduced include all those which are cited in Volumes I and II of this history, except for publications issued at regular intervals.

J.K.H.

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PART I

Before Bretton Woods

The White Plan

The first definitive version of Mr. White's plan for a Stabilization Fund was a mimeographed draft dated April 1942. This covered both the Fund and the Bank. It comprised an Introduction, an Outline of the Articles proposed for the Fund and for the Bank, and extensive commentaries on these Articles. The extract (A) below omits the Articles for the Bank and also the commentary on them except for a section which dealt with "A new international currency."

The final version of Mr. White's plan was issued by the U.S. Treasury in printed form on July 10, 1943. This is reproduced in (B) below.

(A) Preliminary Draft Proposal for a United Nations Stabilization Fund and a Bank for Reconstruction and Development of the United and Associated Nations

(April 1942)

H. D. WHITE, Assistant to the Secretary, U.S. Treasury Department

This report has been prepared at the request of Secretary Morgenthau that I draft a plan for an International Stabilization Fund and an International Unit of Currency.

He felt that the requirements of furthering the war effort and preparing for the financial needs of the reconstruction period called for the immediate preparation and study of preliminary proposals.—H. D. WHITE

INTRODUCTION

Suggested Plan for a United and Associated Nations Stabilization Fund and a Bank for Reconstruction and Development of the United and Associated Nations

It is yet too soon to know the precise form or the approximate magnitude of post-war monetary problems. But one thing is certain. No matter how long the war lasts nor how it is won, we shall be faced with three inescapable problems: to prevent the disruption of foreign exchanges and the collapse of monetary and credit systems; to assure the restoration of foreign trade; and to supply the huge volume of capital that will be needed virtually throughout the world for reconstruction, for relief, and for economic recovery.

If we are to avoid drifting from the peace table into a period of chaotic competition, monetary disorders, depressions, political disruption, and finally into new wars within as well as among nations, we must be equipped to grapple with these three problems and to make substantial progress toward their solution.

Specific plans must be formulated now.

Clearly the task can be successfully handled only through international action. In most discussions of post-war problems this fact has been recognized, yet to date—though a number of persons have pointed to the solution in general terms—no detailed plans sufficiently realistic or practical to give promise of accomplishing the task have been formulated or discussed. It is high time that such plans were drafted. It is time that detailed and workable plans be prepared providing for the creation of agencies with resources, powers and structure adequate to meet the three major post-war needs.

Such agencies should, of course, be designed to deal chiefly with post-war problems. But their establishment must not be postponed until the end of hostilities. It takes many months to set up such agencies. First, a plan has to be perfected. Then it has to be carefully considered by a number of countries. In each country, again, acceptance can follow only upon legislation. That alone will consume many months and possibly longer. And even when the plan is finally accepted, much time will be further consumed in the collection of personnel, and the performance of the preliminary ground work which must be done before effective operations can begin. Altogether, a year may be required before a proposal can be transformed into an operating agency.

Obviously, therefore, even though no important immediate ends will be served by having such agencies functioning during war time, it will be an error to wait until the end of the war is in sight before beginning serious discussion of plans for establishing such agencies. No one knows how soon the war will end, and no one can know how long it will take to get plans approved and the agencies started. Yet, if we are to "win the peace," which will follow the war, we must have adequate economic instruments with which to carry on effective work as soon as the war is over. It would be ill-advised, if not positively dangerous, to leave ourselves at the end of the war unprepared for the stupendous task of world-wide economic reconstruction.

Specific proposals will help win the war.

But there is an additional important reason for initiating at once serious discussion of specific proposals. Such discussion will be a factor toward winning the war. It has been frequently suggested, and with much cogency, that the task of securing the defeat of the Axis powers would be made easier if the victims of aggression, actual and potential, could have more assurance that a victory by the United Nations will not mean in the economic sphere, a mere return to the pre-war pattern of every-country-for-itself, or inevitable depression, of possible widespread economic chaos with the weaker nations succumbing first under the law-of-the-jungle that characterized international economic practices of the pre-war decade. That assurance must be given now. The people of the anti-Axis powers must be encouraged to feel themselves on solid international ground, they must be given to understand that a United Nations victory will not usher in another two decades of economic uneasiness, bickering, ferment, and disruption. They must be assured that something will be done in the sphere of international economic relations that is new, that is powerful enough and comprehensive enough to give expectation of successfully filling a world need. They must have assurance that methods and resources are being prepared to provide them with capital to help them rebuild their devastated areas, reconstruct their war-distorted economies, and help free them from the strangulating grasp of lost markets and depleted reserves. Finally, they must have assurance that the United States does not intend to desert the war-worn and impoverished nations after the war is won, but proposes to help them in the long and difficult task of economic reconstruction. To help them, not primarily for altruistic motives, but from recognition of the truth that prosperity, like peace, is indivisible. To give that assurance now is to unify and encourage the anti-Axis forces, to greatly strengthen their will and effort to win.

Nor will the effect be on the anti-Axis powers alone. Whether within the Axis countries the will to fight would be weakened by such arrangements is not certain, but assuredly it would not be strengthened. And certainly the people in the invaded countries, and the wavering elements in the Axis dominated and Axis-influenced countries would be given additional cause to throw in their lot more definitely and openly with the anti-Axis forces if there is real promise that an orderly prosperous world will emerge from a United Nations victory.

Two International Government Agencies must be established—a Stabilization Fund and a Bank for Reconstruction.

A vital part of that promise rests on international monetary and banking collaboration. The United Nations and the Nations associated with them must undertake cooperatively two tasks as soon as possible: first, to provide an instrument with the means and the procedure to stabilize foreign exchange rates and strengthen the monetary systems of the United Nations; and second, to establish an agency with resources and powers adequate to provide capital for economic reconstruction, to facilitate rapid and smooth transition from war-time economies to peace-time economies, to provide relief for stricken people during the immediate post-war period, to increase foreign trade and permanently increase the productivity of the United Nations.

Those two tasks should be kept distinct. Though in some of their facets and in many of their consequences there is considerable interdependence and interaction, the two are different enough to call for separate instrumentalities. Each is sufficiently specialized to require different resources, different responsibilities, and different procedures and criteria for action. To supply the United Nations with necessary capital not otherwise available except possibly on too costly terms should be the function of a bank created for that specific purpose; whereas monetary stabilization—a highly specialized function calling for a special structure, special personnel, and special organization—would best be performed by a stabilization fund created to perform that special function.

It is therefore recommended that immediate consideration be given to formulating plans for the establishment of two separate institutions:

1. A United and Associated Nations Stabilization Fund, and
2. A Bank for Reconstruction and Development of the United and Associated Nations.

While either agency could function without the existence of the other, the creation of both would nevertheless aid greatly in the functioning of each. Doubtless one agency with the combined functions of both could be set up, but it could operate only with a loss of effectiveness, risk of over-centralization of power, and danger of making costly errors of judgment. The best promise of successful operation seems to lie in the creation of two separate institutions, linked together by one or two directors in common.

Proposals must be drafted by experts of many governments meeting for that purpose.

It is hoped that some time soon, representatives of various interested governments will meet in conference to explore the possibility of working out a plan for the establishment of an international stabilization fund and bank. To facilitate the preliminary work of such a committee, and to provide the officials of the interested governments with a proposal set in specific enough terms to encourage and justify fruitful discussion prior to a meeting, the following report has been prepared. It contains a suggested plan for a fund and for a bank, and also some discussion of the various points involved.

Anyone familiar with the task of setting up new and complex organizations such as the two envisaged will fully appreciate that no single person, no matter how well informed on the subject, can hope to draft a plan that would meet with general approval. This is especially true of a proposal calling for international collaboration and requiring acceptance by several governments. To draft a plan that is likely to meet with approval of various governments is a task beyond the competence even of a group of economists from any single country. The details of any plan submitted for consideration would have to be subjected to careful evaluation and examination by a number of men, some of whom should be expert in the handling of international economic problems and monetary theory, and others at home in related fields. In addition to monetary problems, questions of sovereignty, of national interest, and of broad economic policy are involved in some of the more important provisions, and these inevitably must be the subject of controversy and compromise. They are also matters that must be discussed in detail and at length by high officials whose responsibilities include the shaping and administration of monetary and financial policy.

The proposals and comments that follow are submitted with the intent of providing a starting point for intelligent discussion and of calling attention to some of the difficulties which would have to be satisfactorily met before a workable and acceptable plan may emerge. The proposals have been set forth only in outline and for the most part only those points are included which are essential to an understanding of the plan.

It is certain that some of the powers and requirements included in the outline of the Fund and the Bank will not survive discussion, prejudice and fear of departure from the usual. Some may not stand the test of political reality, and some may be unacceptable on technical grounds, while others may be generally regarded as going too far toward "internationalism." Yet most of them appear as desirable objectives in most writings or conferences on post-war economies and are worth considering.

Willingness to depart from tradition and break new ground is essential if meaningful results are to be obtained.

It will perhaps help toward understanding and induce a more sympathetic approach to the proposals which follow to state at the outset that something much more than the usual banking and stabilization functions are envisaged in the plan. There is urgent need for instruments which will pave the way and make easy a high degree of cooperation and collaboration among the United Nations in economic fields hitherto held too sacrosanct for international action or multilateral sovereignty. A breach must be made and widened in the outmoded and disastrous economic policy of each-country-for-itself-and-the-devil-take-the-weakest. Just as the failure to develop an effective League of Nations has made possible two devastating wars within one generation, so the absence of a high degree of economic collaboration among the leading nations will, during the coming decade, inevitably result in economic warfare that will be but the prelude and instigator of military warfare on an even vaster scale.

The Fund and the Bank described in the following pages are envisaged as economic instruments that most easily and effectively can facilitate that high degree of economic collaboration. It will be at once apparent that the resources, powers and requirements for membership, accorded both agencies go far beyond the usual attributes of monetary stabilization and of banking. They must if they are to be the stepping stone from shortsighted disastrous economic nationalism to intelligent international collaboration. Timidity will not serve. It is my conviction that the long-time effectiveness of both agencies will be measured by the degree to which boldness and vision are displayed in their organization and objectives.

Part I, which follows, consists of an outline of (1) a United and Associated Nations Stabilization Fund, and (2) of a Bank for Reconstruction of the United and Associated Nations.

Part II consists of a brief explanation and discussion of the proposed Fund, and Part III of the proposed Bank.

PART I

A. SUGGESTED OUTLINE OF A UNITED AND ASSOCIATED NATIONS STABILIZATION FUND.

I. The Purposes of the Fund are:

1. To stabilize foreign exchange rates of the United Nations.
2. To encourage the flow of productive capital among the United Nations.
3. To liberate blocked balances.
4. To help correct the maldistribution of gold among the United Nations.
5. To facilitate the settlement and servicing of international debts—both public and private.
6. To shorten the periods of disturbing disequilibrium in the international accounts of member countries and help stabilize price levels.
7. To reduce the necessity and use of foreign exchange controls.
8. To eliminate multiple currency practices and bilateral clearing arrangements.
9. To promote sound note issuing and credit policies and practices among the United Nations.
10. To reduce barriers to foreign trade.
11. To promote more efficient and less expensive clearings of international exchange transactions.

II. Powers.

To help attain the objectives listed above, the Fund shall have the following powers:

1. Buy, sell and hold gold, currencies, foreign exchange, bills of exchange, and government bonds of the "member" countries, and act as a clearing house for international movement of funds, balances, checks, drafts, acceptances, gold.
2. The Treasury of each member country (or its agent, a stabilization fund or central bank) shall have the privilege of purchasing from the Fund the currency of any member country which the Fund holds, provided:
   a. The currency demanded from the Fund is required to meet adverse balance of payments to the country whose currency is being demanded.
   b. The sum in the Fund of the currency of the country making the purchase shall be, after adding the sum proposed to be purchased, not more than

100 percent of the total sum—gold, currency, and notes—originally contributed to the Fund.

c. The rate of exchange shall be the one determined by the Fund.

3. Should a country wish to sell its currency to the Fund in an amount in excess of the above quota, approval by four-fifths of the member votes would be required. The Fund could decide to purchase the excess of the currency in question if:

   a. It is believed the anticipated balance of payments of the country in question was such as to warrant the expectation that the "excess" could be disposed of within a reasonable time, or

   b. The country in question had gold holdings which, together with gold it expected to accumulate within a reasonable time, were adequate to replace the excess, and

   c. The country in question agreed to adopt and carry out measures designed to correct the disequilibrium in the country's balance of payments, which the Fund recommended—after careful examination of the situation.

4. The governments of member countries may sell to the Fund, blocked foreign balances acquired from their nationals, provided all the following conditions are met:

   a. The foreign balances were in member countries and were either partly or wholly blocked.

   b. The foreign balances were included in the sum reported (for the purpose of this provision) by the member government as blocked on date of its becoming a member.

   c. The country selling the blocked balances to the Fund agreed to begin repurchasing 40 percent of the amount sold to the Fund, at the price received, and at a rate not to be less than 2 percent a year. The repurchases to begin not later than three years after date of sale, and the currency to be used in repayment to be either the currency received or the local currency, as desired by the Fund.

   d. The country in which the blocked balances are held agrees to transfer those balances to the Fund, and purchase back 40 percent of them from the Fund, at the rate of 2 percent a year, beginning not later than three years after the date of transfer. The Fund may accept government bonds payable in gold in lieu of part of the blocked balances, and shall be free to sell such bonds under certain conditions.

   e. If the country selling the blocked foreign balances to the Fund asks for foreign exchange rather than local currency, it must need the foreign exchange for the purpose of meeting adverse balance of payments arising from any cause except acquisitions of gold, or accumulation of foreign balances.

   f. The country in which the blocked funds are kept agrees not to impose any restrictions on the installments of the 40 percent portion gradually to be repurchased by country owning the blocked balances.

   g. A charge of 1 percent, payable in the currency of the country paying shall be levied against the country selling its blocked funds, and a charge of 1 percent payable by country in which blocked account exists.

h. The Fund shall determine from time to time what shall be the maximum proportion of the blocked balances it can afford to take over under this provision.

i. The Fund on its part agrees not to sell the blocked balances acquired under the above authority, except with the permission, or at the request of the country in which the blocked balances are being held but can invest those balances in regular or special government securities of that country.

5. The Fund would fix the rates at which it will exchange one member's currency for another, and the rates at which it will buy and sell gold with local currencies. The guiding principle in the fixing of such rates shall be stability in exchange relationships. Changes in the rates shall be made only when essential to correction of a fundamental disequilibrium, and only with the consent of four-fifths of member votes.

6. The Fund shall have authority to deal only with the Treasuries of the participating countries, or with official stabilization funds of those countries, and with the bank designated by participating government as its fiscal agent, and with international banks owned by governments.

7. The Fund shall not have the authority to engage in any transactions within a member country, or with any corporation or part of the government of that country without the consent of the Board representative of that country.

8. The Fund shall have the authority to buy and sell currencies of non-member countries, but shall not be authorized to hold such currencies beyond sixty days after date of purchase, except with the approval of four-fifths of the member votes.

9. The Fund shall have the authority to borrow, at such rates as the Fund may recommend, the currency of any country, provided four-fifths of the member votes approve the terms, amount and condition of such borrowing.

10. The Fund shall have the authority to invest any currency it holds in "short-term" securities—commercial or government—of the country of that currency provided a four-fifths vote of the member votes shall approve, and provided further that the approving votes shall include that of the Board representative of the country in which the investment is to be made.

11. The Fund shall have authority to sell the obligation it holds of the member countries provided four-fifths of the member votes approve, and provided the representative of the country in which the securities are to be sold approves.

12. No sale of any currency from the Fund shall be made to a member without approval of four-fifths of member votes when the currency so sold is to be used or is to make possible adjustment of a foreign debt, including, of course, debts already in default.

13. Any member country can borrow local currency from the Fund for one year or less up to 75 percent of the currency of that country held by the Fund, provided such loan is approved by three-fourths of the member votes. A country borrowing such funds shall pay to the Fund an interest rate of 1 percent a year.

14. A very moderate service charge shall be made by the Fund on all exchange and gold transactions.

III. Eligibility for membership.

Any member of the United or Associated Nations is eligible for membership in the Fund provided it agrees:

1. To abandon, not later than one year after joining the Fund, or after the cessation of hostilities, whichever is later, all restrictions and controls over foreign exchange transactions with member countries, except with the approval of the Fund.
2. To alter exchange rates on the currencies of other countries only with the consent of the Fund and only to the extent and in the direction approved by the Fund, with the exception of a narrow range fixed by the Fund and permitted to all member currencies.
3. (a) Not to accept or permit deposits or investments from any member country except with the permission of the government of that country, and
   (b) To make available to the government of any member country at its request all property in form of deposits, investments, securities of the nationals of that member country.
4. Not to enter upon any bilateral clearing arrangements.
5. Not to adopt any monetary or general price measure or policy, the effect of which, in the opinion of a majority of the member votes, would be to bring about sooner or later a serious disequilibrium in the balance of payments, if four-fifths of the member votes of the Fund submitted to the country in question their disapproval of the adoption of the measure.
6. To embark upon a program of gradual reduction of existing trade barriers—import duties, import quotas, administrative devices—and further agree not to adopt any increase in tariff schedules, or other devices having as their purpose higher trade obstacles, without giving reasonable opportunity for the Fund to study the effect of the contemplated change on exchange rates and register its opinion. In rendering its opinion, the Fund will make recommendation to which the member governments agree to give serious consideration.
7. Not to permit any defaults on foreign obligations of the government, Central Bank or government agency without approval of the Fund.
8. Not to subsidize—directly or indirectly—the exportation of any commodity or services to member countries without consent of the Fund.

IV. Composition of the Fund.

1. The Fund shall consist of gold, currencies of member countries, and member government securities in such amounts as shall be indicated by a formula set forth in the agreement.

   The total subscription to the Fund shall be the equivalent of at least $5 billion. The Bank of the United Nations should subscribe $100 million to the Fund.
2. The contribution of each country shall consist of 25 percent cash and 25 percent in interest-bearing government securities (interest and principal payable in gold or its equivalent). The remaining 50 percent to be paid in such installments and in such form as shall be determined from time to time by the Fund.

   The initial payment of 25 percent cash shall consist of at least one-half in gold, the remainder in local currency.

V. Management.

1. The management of the Fund shall be vested in a Board of Directors consisting

of the representatives appointed by the member governments. Each government shall appoint one representative.

2. The Board shall elect a chairman and a small operating committee. The Chairman shall be chief of the operating committee. The members of the operating committee should devote full time to the management of the Fund, should be assisted by an appropriate technical staff, and should receive an adequate salary. The Chief of the operating committee with the approval of the Board shall appoint the heads of the departments.
3. In all voting by the Board each representative shall have one hundred votes, plus one vote for the equivalent of every million dollars subscribed to the Fund by his government.
4. A country can replace, wholly or in part, its bonds with currency or gold. The number of votes its representatives can cast will alter accordingly.
5. All decisions, except where specifically provided otherwise, shall be decided by the majority of the votes cast.
6. The President of the Bank for the United Nations shall be a member of the Board and shall have 100 votes. He shall have no additional votes notwithstanding the Bank's participation in the Fund.

VI. The rules and regulations regarding the type, amount and conditions of day-to-day transactions to be handled by the operating committee, shall be promulgated by four-fifths of the member votes.

VII. No change in the gold value of any currency of the participating countries shall be permitted to alter the gold value of the total currency holdings in the Fund. Thus, if the currency of any of the participating countries should depreciate, that country must deliver to the Fund an amount of its local currency equal to the decreased value of that currency held by the Fund. Likewise, if the currency of a particular country should increase, the Fund must deliver to that country an amount (in the currency of that country) equal to the resultant increase in the gold value of the Fund's holdings. This provision does not apply to currencies acquired under paragraph 4 under section on "Powers."

VIII. A country failing to contribute to the Fund sums due the Fund shall be dropped as a member, provided a majority of the member votes so decide. Any member dropped shall have returned to it an amount (in its own currency) equal to its contribution minus any sum due by that country to the Fund.

IX. Net profits earned by the Fund shall be distributed in the following manner:

1. 50 percent to reserves until the reserves are equal to 10 percent of the assets of the Fund.
2. 50 percent to be divided each year among the members in form of the local currency. That is, each country shall distribute its dividends in its own currency.

X. The member governments agree to furnish the Fund with all information it needs for its operations, and to furnish such reports as it may require, in the form and at the times requested by the Fund.

[Part I.B, outlining proposals for an International Bank, has been omitted here.]

PART II

A UNITED NATIONS STABILIZATION FUND

The outline of the purposes, powers and structure of a stabilization fund presented in the previous pages is hardly enough to supply the interested reader with more than very general idea of how the proposed institution would function and what they would be expected to accomplish. A brief discussion of some of the points outlined should serve to give a clearer idea of what is proposed, and also suggest some of the difficulties involved in the proposal.

In the following pages the outline presented in Part I is somewhat elaborated and some brief discussion is ventured of the more troublesome or important points. This section is devoted to discussion of the Fund and Part III to discussion of the Bank.

I. Purposes of the Fund

The various purposes enumerated in the outline are to a considerable extent interdependent and overlapping and in some instances may even represent apparently conflicting tendencies. Yet, progress in the attainment of almost any one of them facilitates progress toward the attainment of many of the others. Each of them represents a different phase of international monetary arrangements and calls in the main for different procedure, different powers, and in some cases, different kinds of resources.

The fact that some of the objectives may be at times harmonious and at other times conflicting, indicates that the management of an international stabilization fund cannot be reduced to a matter of simple rules. The successful operation of the Fund calls for constant examination of a large variety of pertinent factors and the continual evaluation of various effects which might be expected to follow any particular action or failure to act.

There follows a brief amplification and justification of each of the objectives.

Stabilization of foreign exchange rates.

The advantages of obtaining stable exchange rates are patent. The maintenance of stable exchange rates means the elimination of exchange risk in international economic and financial transactions. The cost of conducting foreign trade is thereby reduced, and capital flows much more easily to the country where it yields the greatest return because both short-term and long-term investments are greatly hampered by the possibility of loss from exchange depreciation. As the expectation of continued stability in foreign exchange rates is strengthened there is also more chance of avoiding the disrupting effects of flights of capital and of inflation.

Altogether, if the Fund were successful in bringing about a much greater degree of stability in foreign exchange relationships than existed during the 'twenties and 'thirties, it will have justified its existence on that score alone.

Flow of productive capital, blocked balances, and redistribution of gold.

The desirability of encouraging the flow of productive capital to areas where it can be most profitably employed needs no emphasis. The Fund can help encourage that flow by reducing exchange risks, and also by making the imposition of restrictions on exchange transactions less likely to happen. Also, insofar as the Fund can help strengthen the monetary and banking system of the country, it increases that country's attraction to funds of private foreign investors.

Balances owned by residents of another country which have been blocked because holdings of gold and other liquid foreign exchange assets are inadequate (this does not apply to the United States where restrictions have been imposed for reasons other than because of any scarcity of gold reserves) will constitute after the war one of the danger spots to monetary stability, and to resumption of liberal trade policies. If the Fund can eliminate that danger spot it will have justified its existence—even were it to accomplish little else.

The Fund has the possibility of utilizing more effectively the gold resources of any given country, and thereby encourage countries to hold larger gold reserves. By facilitating an easier adjustment of the international balance of payments, it reduces the volume of hectic gold movements. Machinery can be developed under the aegis of the Bank, with which countries can more easily develop a favorable balance of payments vis-à-vis the gold-holding and producing countries. By providing strength to countries with weakened economic and credit systems, the Fund can also encourage the return flow of gold from the United States.

Servicing of international debts.

The reduction in risk of exchange loss and progress toward elimination of restrictions on foreign exchange transactions should make easier debt adjustments of foreign debts now in default—both public and private—and continued servicing of debts not in default.

To help stabilize price levels.

Any development which would contribute toward stability of price levels is greatly to be welcomed. Wide swings in price levels are one of the destructive elements in domestic as well as international trade. An intelligent use of an international stabilization fund could contribute something toward reducing the fluctuations, and even the cyclical movements of prices within a country and in the relationship of price levels between countries.

To reduce the necessity and use of foreign exchange controls.

Foreign exchange controls usually constitute an interference with trade and capital flows. Unfortunately, such controls are too often preferable to the alternatives facing a particular country. Insofar as an international stabilization fund can reduce the necessity for such controls and can prevent the use of such controls where they are not necessary, it will serve to substantially increase foreign trade of nations and encourage the flow of production capital.

To eliminate multiple currency practices and bilateral clearing arrangements.

The developments during the last twenty years of multiple currency devices and bilateral clearing arrangements served to disrupt trade, increase economic difficulties in some countries, and stimulate the worst kind of competitive practices among countries seeking to increase their foreign markets or protect the foreign markets they already have. These practices frequently arise from difficulties which are subject to mitigation by an appropriately handled stabilization fund. An international stabilization fund with ample resources and broad powers could do much to eliminate the justification for resorting to trade practices that are an obstacle to a high level of foreign trade for all countries.

Promotion of sound note issuing and credit policies and practices.

The sounder the monetary and banking policies of governments, the less sensitive are they to economic disturbances, and the quicker will be the recovery from any depression. There are numerous ways in which an international stabilization fund could add to the strength of monetary systems of member governments.

Reduction of trade barriers.

The existence of high tariff policies and other obstacles to trade and the tendency during the post-war period to heighten those barriers, are serious barriers to recovery and maintenance of a high level of economic activity among countries. It will be readily admitted that if an international stabilization fund can assist in bringing about a reduction in the unnecessary barriers to international trade, it will have performed a valuable service toward maintaining business recovery after the war.

The establishment of an efficient clearing house for international monetary transactions.

The advantage of providing such a clearing house would not be negligible, particularly among countries who transact a small volume of business with each other. The spread between the buying and selling rates of some foreign currencies is much larger in some countries than it should be. Thus transactions between those countries are subject to handicaps that are unnecessary. To the extent that exchange rate spreads are adjuncts to fiscal or commercial policy, the Fund will deal with the problem in other ways. It is impossible to measure the gains that accrue from more efficient handling of clearances, but they could be substantial.

Can these objectives be reached?

Each of the objectives listed, if achieved, would help in some degree to restore and maintain world prosperity. If the Fund is to make much progress toward achieving the objectives enumerated in the previous pages, it must have broad powers and courageous and intelligent direction. It is a task that is surely within the competence of the present generation.

II. Powers of the Fund

The Fund should have the power to buy, sell and hold gold, currencies, foreign exchange, bills of exchange, and government securities of the "member" countries and act as a clearing house for international movements of gold and balances.

The purchase and sale of gold would be an essential part of the operations of the Fund. The Fund might well become the most attractive depository for earmarked gold, and be the means of greatly reducing the need for physical transfers of gold among members.

To promote the practice of "earmarking" gold its storing and transfer could be made without charge to members, and agreement between countries could accord a maximum of legal security to such holdings. It should even be possible to secure written assurance by the government of the country where the gold was to be held that such gold would not be subject to any controls. Earmarked gold could be given a special status so that countries could unhesitatingly earmark large amounts with the Fund and still record such gold as part of their own reserve. The Fund might find it convenient to have a branch office on each continent. This would still further cut down gold shipments. It would also speed up other kinds of transactions.

Dealings in foreign exchange would constitute, of course, the chief business of the Fund. It is through such transactions that the Fund would be expected to carry out many of its objectives. It might therefore be helpful if this part of the Fund's operations were described with little more detail. Tedious though it may be, this part of the Fund's activities must be elaborated to permit a proper evaluation of the role an international stabilization fund can play. In the several pages which follow the exchange operations with which the Fund would be chiefly occupied are briefly described.

The Treasury, or its fiscal agent, of each member country shall have the privilege of purchasing from the Fund the currency of any member country which the Fund holds.

Since the Fund would deal only with and for Treasuries (or their fiscal agents and the Bank) the regular private channels through which foreign exchange transactions are now consummated by commercial banks, and other dealers and brokers, would continue to serve. It is presumed that the Treasuries would deal in foreign exchange only when exchange situation warranted government operation. They might also employ the Fund to transact foreign exchange business between governments.

Certain restrictions on operations are necessitated by the wide differences in the strength of the various currencies. If any country could purchase from the Fund as much of any currency as it pleased at a fixed rate without reducing the supply of the strong currency available in the open market, countries with weak currencies would be tempted to accumulate stocks of strong currencies. The Fund's supply of gold and strong currencies would soon be depleted and in their place would be weak currencies, i.e. currencies of countries which prefer other currencies to their own. Some restrictions are therefore necessary.

The first condition of purchase from the Fund might be that the currency purchased must be needed to meet an adverse balance of payments to the country whose currency is being demanded. Thus, a country could not obtain gold or other currency from the Fund if the direct result were to increase the gold or foreign exchange holdings of the Government, its Stabilization Fund, or fiscal agent, except, of course, possibly for short periods.

There would be no justification for a member government to use the Fund's assets as a means of converting its currency into gold or foreign exchange, unless it needed that gold or foreign exchange to meet claims or liabilities due or soon to be due. It is quite true that one of the possible reasons why a government would need more foreign exchange might be that its nationals were building up their foreign balances, or increasing their foreign investments. That, however, is a quite different matter than the government or Central Bank building up its foreign balances. The Fund might wish to supply the foreign exchange when the demand arises from an outflow of private funds. Whether or not it would wish to do so depends on a number of factors, including the cause of the outflow, the rate of outflow, the countries involved, the reserve position of the capital losing country, and the rapidity with which the mechanism of adjustment in the balance of payments is operating. Each episode would have to be considered on its own merits. It is, therefore, important that when there is present in the balance of payments of the country in question substantial outflow of capital which may be contributing to the disequilibrium the Fund have the authority to provide the exchange or not, as it sees fit. It would have this authority in any case, as indicated below, if the country in question had already obtained its maximum quota of foreign exchange from the Fund but the Fund should also have the privilege of not responding to demand for exchange, even before the quota was reached, where capital movements are involved.

What this matter boils down to is that the Fund should have the authority to determine whether the transactions causing a balance to turn unfavorable include transactions which the Fund would judge "illegitimate" under the circumstances. There are times when some types of capital outflow for some countries would be considered "legitimate," whereas the same type for other countries or even for the same country under different circumstances would be regarded as "illegitimate." There might also be instances in which all types of capital outflows for a given country might be considered "illegitimate," whereas for another country, all types might be considered "legitimate." No generalization can be made without all the circumstances being given. It is necessary only that the Fund have authority to make the decision on this matter and, as explained later, that the Fund have the authority to obtain the kind of information that would enable it to make an intelligent decision.

To aid in the settlement of international balance is the legitimate use of the Fund and this use is in no way interfered with by the above restriction. Better information on foreign balances and volume of exchange transactions than is now available in most countries will be necessary before it will be possible for the Fund to operate wisely under this restriction, but the development of such statistical data should not be difficult, especially since exchange controls in most countries are prevalent.

The restriction that the foreign exchange should be needed to meet adverse balances is not enough, however, to protect the strong assets of the Fund. If that were the only restriction imposed, a country could continue for a long time to permit an unfavorable balance of payments without calling forth the usual restraints. Without additional restrictions the Fund would in effect be placing the entire gold and foreign exchange assets at the disposal of any member country. The purpose of the Fund could not be to supply an unlimited amount of foreign exchange to any country which might not wish to adopt the proper measures to correct a prolonged disequilibrium in its transactions with foreign countries.

The sum in the Fund of the currency of the country making the purchase shall be, after adding the sum proposed to be sold to the Fund, not more than 100 percent of the total sum (currency, gold and notes) originally contributed to the Fund.

A quantitative limit is therefore also necessary on the amount of foreign exchange a country could purchase from the Fund, without special action.

What limit it were best to set is difficult to decide. It should be large enough to take care of fluctuations in the country's balance of payments that occur within a year or two, but should not be so large as to make it unlikely that the currency sold to the Fund would be repurchased by the country in question within a reasonable time. It is suggested that a country should be able to purchase with its currency any other country's currency so long as the Fund's holdings of the purchasing country is not more than 100 percent of that country's original total contribution to the Fund. Since one-fourth of the original contribution was in form of gold (plus ¼ in local currency and ½ in notes or bonds) the 100 percent increase in the holdings of the Fund actually represents an increase of 300 percent of the local currency subscribed. In other words, a country subscribing $100 million, consisting of $25 million gold, $25 million local currency, and $50 million obligations would be able to buy with local currency as much as $75 million of any currency needed. Since $25 million of gold had been subscribed, the net immediate possible gain to the country needing foreign exchange would be $50 million of foreign exchange. That may seem a small sum and doubtless is for some countries. However, it should be noted the limit is not a rigid nor final one. It is supplemented by an important qualification, to be described in a moment.

How the assistance by the Fund would operate may be more easily understood by following through the steps of a transaction using a simplified illustration:

The Government (or fiscal agent) of Country A finds that the demand by its nationals for foreign exchange, arising out of trade and service transactions, is increasing relative to the supply, to the point where it must (a) give up more gold than it feels desirable, or (b) impose restrictions on imports—either through exchange controls or import controls, or (c) permit its currency to depreciate. In that situation, being a member of the Fund, it turns to the Fund for the assistance it is entitled to receive.

It purchases from the Fund as much of the types of currencies it needs, paying for it with its own currency. This it can do as its right so long as the sum of its currency which the Fund possesses is not in excess of 100 percent of Country A's original total contribution.

Sooner or later other countries will turn to the Fund to buy currency of Country A, and Country A will then again be able to buy other currencies from the Fund if necessary. It might happen that a long time would elapse before Country A's balance of payments would turn favorable (i.e. before Country A's inpayments exceeded her outpayments so that some stabilization fund or central bank would be confronted with the same choice vis-à-vis Country A that Country A had been earlier). So long as Country A had not used up its maximum allowance permitted without special decision by the Fund, the duration of the period during which Country A would not be decreasing the Fund's holdings of her currency would not matter very much.

If the balance of payments position among all the member countries did not stray from equilibrium by large amounts (relative to their foreign exchange assets) or for long periods, then the Fund would serve as a sort of reserve pillow absorbing the shock of pressures on exchange rates, thus safeguarding trade from unnecessary restrictions and exchange from unnecessary fluctuations. But it would be unwarranted to expect all the balance of payments situations to return quickly to equilibrium. For some countries it would frequently happen, and for almost all countries it would sometimes happen that an adverse balance of payment situation would persist. There are a number of reasons for this, but it would take more space to explain them than is justified in this report. Suffice to say that it would be wholly to be expected that some member countries would frequently find they have sold so much of their currency to the Fund that the Fund held the maximum permitted by usual majority procedures. When that point will have been reached by any country it will have already obtained substantial assistance.

Let it be assumed, for example, that Country A had originally contributed $100 million to the Fund, and due to the development of an adverse balance it has sold to the Fund $75 million in addition to the $25 million originally subscribed. When that point is reached Country A will have received what is virtually a costless "loan" of $50 million of other countries' currencies. It really is not a loan since Country A has given its own currency in exchange, yet Country A has been able to buy $75 million of foreign exchange with its own currency, whereas without access to the Fund it would have had to use gold or other foreign exchange resources. Since Country A has subscribed $25 million in gold to the Fund which it otherwise could have used to purchase foreign exchange the gain it is able to make through its membership in the Fund is the use of an additional $50 million. That, however, need be only the beginning.

There is a provision which permits the Fund to increase its purchase of Country A's currency after the above-described maximum is reached, as follows:

A country can exceed the limit imposed by the regulation provided it can obtain approval of four-fifths of the member votes.

This approval should be given only if four-fifths of the member votes were of the opinion that (a) the anticipated balance of payments prospects of the country in question were such as to warrant the expectation that the "excess" could be disposed of within a "reasonable" time, or (b) if the country in question had gold holdings which together with the gold it expected to accumulate within a reasonable time was adequate to replace the excess, and (c) if the country in question agreed to adopt and carry out measures designed to correct the disequilibrium measures which the Fund either approved or suggested, and (d) some time limit be imposed on the country during which the excess shall be repurchased—a time limit that shall be long enough to permit the country to adjust its international accounts without too great a strain.

This provision gives the desired flexibility. No country need suffer from lack of foreign exchange necessary to meet temporary drains. It need not even suffer from shortage of foreign exchange during a prolonged period of disequilibrium provided the Fund was satisfied proper steps were being taken to restore equilibrium.

Admittedly the operation of that flexible provision would call for technical knowledge, careful examination and good judgment by the Fund's staff. It is hoped that the technical staff which the Fund would gradually develop would be the most competent available in that special field. It would need to be because the problems it will have to deal with are difficult and because the success of the Fund in reducing fluctuations in foreign trade and in preventing monetary disturbances will depend largely upon the wisdom of the technical staff's advice. The Fund would doubtless be free from political pressure from any one country in its decisions, and should be able to make recommendations more apt to be in the long-run interest of the country concerned, than would likely be the case where decisions are dominated by short-run considerations or by domestic political considerations.

To what extent the Fund will be called upon to purchase and accumulate local currencies cannot be forecast. It depends on a number of changing factors, such as: how many countries will participate in the Fund, and how much each will invest; how rapidly foreign exchange controls will be eliminated; how much capital will be available for foreign investment, and finally, the pattern of world trade which will emerge shortly after peace is resumed.

Much also will depend on the extent to which some of the countries have foreign balances to which they will prefer to resort when experiencing adverse balances. That will mean that the Fund will not be able to convert some of the currencies which it had acquired as rapidly as would seem to be called for by the then-prevailing pattern of trade. Thus, for example, the Fund may accept sterling from England because England has turned to the Fund to meet an adverse balance of payments. Other countries, however, later developing adverse balances with England might not turn to the Fund for sterling. They might utilize sterling balances which they already have, or dip into ample gold holdings. The Fund would in that case be unable to diminish its holdings of sterling and therefore England would not be able to sell the Fund more sterling later if necessary except by action under the flexible provision.

The fact that the countries which will participate to the largest extent in the Fund are likely to be those least in need of resorting to the Fund for assistance of the character indicated above, would make it possible for the Fund to help most where it would be most needed. Only experience can show how far the Fund could go in eliminating fluctuations in exchange rates and in making the imposition of exchange and trade controls unnecessary. It is certain that the Fund cannot perform miracles, nor solve all problems involved in the maintenance of equilibrium in international accounts. The Fund cannot and should not make it possible for countries to ignore the cardinal principle of international economic relations, namely, that a country must in the long run buy only as much goods and services as it sells. An important exception, of course, is a country which has a balance due it on current borrowing, but sooner or later even that country will have to sell more than it buys in order to pay interest and principal on its borrowings. To be sure, the country which has foreign exchange resources, in the form of gold or income from foreign investments, can continue to buy more than it sells so long as those resources last, but for most countries these resources are not present in abundance, and hence for most countries the Fund can operate to make their path much smoother provided the countries themselves approach their own balance of payments problem intelligently.

Gold producing countries would not be immune from needing help from the Fund. It is true that such countries usually have an "unfavorable" balance of payments in the sense that they need constant exports of gold to help pay for the exchange they need. But such countries may and frequently do need more foreign exchange than they can buy with current gold production. At such times they can be helped by the Fund just as can countries which do not produce gold.

Even if countries ignore the basic limitations set upon any country's ability to buy more than it sells, the Fund can exercise considerable influence in helping them to correct this situation in time, and in ways which will create the smallest amount of destruction to world trade and least disturbance to their own economy.

It may be that experience will demonstrate that the limitations set upon the Fund's authority to agree to purchase currencies offered it are too strict. It may be that the commercial policies pursued by numerous countries, including more liberal tariff policies, will reduce the length of time in which countries are apt to experience adverse balance of payments and also the magnitudes of the disequilibrium. If so, the Fund can undertake much greater obligations. In any case the Fund is well protected against loss.

It should be remembered that the Fund in its operations is not undertaking the same risk of loss that would be involved in a usual extension of credit. The Fund gets foreign exchange in return for the currency it gives up, and each member government is required to make good any exchange loss suffered by the Fund through depreciation of its currency. Thus, the Fund not only has the foreign exchange which is always worth something, but it also has the obligation of the government to make good any exchange loss that might result. More than that, each government has invested with the Fund gold, currency, and its obligations, which the Fund would, in effect, have as collateral against potential exchange losses.

The Fund would receive additional protection against loss from the fact that a member government not meeting its obligations to the Fund could be dropped. Without knowing how many members will participate or how influential the Fund will become, we cannot say how serious a punishment being dropped from the Fund would be, but it is not unlikely that it would be serious enough to induce any country to make good its obligations to the Fund, difficult though that might prove to be.

Because the Fund will be undertaking so little risk, it can go further in the assistance it gives to foreign countries than would be the case were the risk of loss great. Should the Fund find itself pressed for certain kinds of currencies, it has of course both assets and borrowing power which can, if necessary, be used to purchase the desired currencies.

The power of the Fund to deal in the bonds of participating governments is an important one. It would, for example, make it possible for the Fund to come to the aid of any country which is being subjected to pressure on its exchange arising out of some types of capital flights. The Fund could, of course, buy the currency of the country, but the circumstances might, under certain conditions, be better handled by buying bonds and it might even help countries which for one reason or another do not have or cannot exercise adequate open-market powers and whose money market has become unduly tight because of a capital flight.

Unfreezing of blocked funds.

Special powers are called for to deal with the problem created by the growing magnitude of blocked balances. The countries in which large totals of balances are blocked are the United States and England (Germany is, of course, excluded) whereas the countries to whom those balances belong include almost the rest of the world.

The balances blocked in the United States present no monetary problem. They were not blocked because of any scarcity of gold or foreign exchange assets and their unblocking will not leave the United States short of gold or foreign exchange poor. There will doubtless be many cases in which for political or legal reasons, unfreezing will be delayed, but the cause of the delay will not be any scarcity of gold which may safely leave the country. There are more than two billion of earmarked gold, three billion of deposits, and possibly several hundred million of short-term investments, the withdrawal of which has been placed under some restrictions. A rapid withdrawal of any part of it, or all of it, can be handled with the utmost ease by the United States because of its large gold reserves. At most, it may prove necessary to lower reserve requirements to prevent a tightening of the credit situation here—should the outflow be great enough. With the cessation of war the release of dollar funds (equivalent to gold) capable of purchasing goods anywhere will prove a very important factor in stimulating trade and aiding reconstructions. The trouble, if any, is apt to be that nationals and governments of foreign countries will not elect to withdraw their funds from the United States rapidly enough.

The situation with respect to blocked balances in England is quite different. The gold and foreign exchange reserves which England will have at the close of the war are certain to be far too small relative to the sterling balances blocked there to permit England to remove restrictions on the withdrawal of funds by foreign owners. England may end the war with more than 5 billion dollars of deposits belonging to residents of other countries, while her liquid foreign exchange resources are likely to be much less than that. Moreover, England will need whatever gold she will be able to accumulate, and indeed should have more foreign exchange available than she is likely to have, in order to operate properly even were the total of foreign balances in England much smaller. Most of these balances belong to the Dominions who would wish to keep substantial sums in England in any case—unless there was imminent danger of sterling depreciation. Against some of the remainder there are offsetting blocked currencies. Nonetheless, the drain on British foreign liquid exchange reserves could easily be greater than England could safely permit.

The unblocking of these sterling funds is highly to be desired. Probably, no single action would do more to stimulate world trade, prevent pressure on numerous exchanges, and reduce the probability of widespread depreciation of currencies. The restoration of confidence in the soundness of British currency, the assurance that international monetary problems are to be intelligently handled, and renewed hope that currency stability will be achieved after the war that would follow a successful unfreezing of sterling, would alone justify every effort to solve through international action the problem of blocked balances in Britain.

The Fund would seem to be the appropriate agency to use for the solution of that problem. The method that could be employed to accomplish this is a bit complicated to describe and may seem at first reading difficult to follow but the importance of the subject warrants the attempt.

To accomplish a maximum of results with a minimum of risks the Fund should be given the power to purchase sterling, or any other currency offered to it, from any country other than the country whose currency is being purchased, provided:

a. The government selling its foreign balances (blocked in another country) to the Fund under this provision guarantees to repurchase 40 percent of the currency from the Fund at the price paid. The repurchase to begin after 3 years and to be made at the rate of not less than 2 percent a year of the amount acquired by the Fund under this authority.

b. The country whose local currency belonging to residents of another country is being offered for sale to the Fund agrees first to transfer title to the balances from the foreign nationals to the Fund, and to begin 3 years after sale to repurchase from the Fund 40 percent of the sterling acquired under this provision at a rate of not less than 2 percent a year, at the purchase price.

c. Not more than 20 percent of the currency offered should be paid for by the Fund with gold, half of which should be exempt from the condition imposed in paragraph (d) below.

d. The particular currency paid over by the Fund in exchange for the currency offered should be either local currency or currency needed by the country to meet an adverse balance of payments, with the exception of the 10 percent of gold. Thus, for example, if Canada wishes to sell to the Fund some of its blocked sterling balances in exchange for United States dollars, Canada would either have to accept Canadian dollars or the Fund would have to be assured that Canada needs the United States dollars to make payments to the United States (for trade, services, interest payments, or even investments) and not to make possible an increase in Canada's gold holdings or an increase in her United States dollar exchange. In other words, if Canada wished to use the sterling accumulated by herself, or her nationals, to convert into funds to be spent in United States, or in Mexico or in Netherlands, the Fund could make that possible without, on the one hand, putting any strain on England and, on the other hand, without denuding the Fund of its gold assets. Canada would be able, according to the above provision, to add to her gold holdings by 10 percent of the blocked balances she sold to the Fund.

e. If the Fund's stocks of sterling or other currencies should decline the Fund can offer to reduce the rate of repurchase required of both governments as specified above, but should it do so, the countries involved must be relieved by the same percentage, and shall be deemed to have repurchased the amount by which they are so released.

A service charge of possibly 1 percent would be imposed by the Fund on countries involved.

Perhaps the operation would be more easily understood if the specific steps were outlined which a country would have to go through under the plan suggested to realize on its blocked funds.

For convenience of illustration, let us take a specific case. Let us assume that the Chinese Government has £50 million blocked in England and wishes to utilize £10 million of it in the ensuing quarter. The steps would be as follows:

1. China makes application to the Fund. The Fund after investigation is satisfied that the use of at least 90 percent of the £10 million is not to accumulate gold or foreign exchange. (China can if it wishes add 10 percent of the £10 million of gold to her holdings.)
2. The £10 million is transferred by the British banks from the Chinese Government to the Fund. The Chinese Government pays 1 percent (in yuan) to the Fund and the British pay 1 percent (in sterling) as a "service" charge.
3. The Fund gives to China
   a. the equivalent of £1 million in gold (if China wishes it), and
   b. the equivalent of £9 million in one or more currencies needed and requested by China—say, $12 million in United States dollars and 120 million Mexican pesos. If the Fund doesn't have enough Mexican pesos, it purchases what it needs.
4. After three years from the date of the transaction:
   a. China begins to repurchase from the Fund each year £200,000 (2 percent of 40 percent of £10 million) of British sterling, at the same rates of exchange she received, paying for the sterling either in yuan or other currencies she received, depending upon the wishes of the Fund.
   b. England begins to repurchase the same amount of sterling each year, paying for the sterling either gold or "New International Units".
   c. China is free to do what she likes with her repurchased sterling, England having agreed in the first place that there would be no restrictions on its withdrawal.
5. Not later than 23 years after the transaction the situation would be as follows:
   a. China would have utilized the £10 million, while her balance of payments would be burdened not at all for 3 years and by not more than 1.2 percent of the £10 million a year after three years.
   b. England would have been able to unfreeze China's balances, while imposing no burden on her (England's) foreign exchange resources for the first three years, and from then on 1.6 percent to 3.2 percent a year (2 percent of from 40 to 80 percent), depending upon what China elects to do with her repurchased 2 percent.
   c. The Fund will have first exchanged some of her gold assets for £1 million, or possibly more if she had to purchase currencies with gold to satisfy China's demands, and will have exchanged the remainder of the £10 million of various currencies for sterling.

      Then the Fund would get back each year gold from England to a sum not less than 2 percent of £4 million until the Fund will have received £4 million in gold. The Fund would also get £4 million of certain currencies from China, leaving the Fund with 2 million pounds sterling.

      The Fund will also have earned 2 percent (1 percent in yuan and 1 percent in sterling) in the transactions, and some interest on her investment of sterling balances in British Government securities.

At the end of 23 years—or sooner if England permits—the Fund could sell the remaining £2 million of sterling and the transaction would be complete.

The above is the transaction under most unfavorable conditions. A more likely outcome is that either or both China and England could purchase back the sterling from the Fund a great deal sooner than 23 years. Nonetheless, a long period is permitted to assure an easy adjustment for both England and China in the event the situation would not be favorable to a rapid adjustment.

The illustration has been that of Government-owned funds. If, as is equally likely, the British sterling balances were owned by nationals of China instead of the Government of China, the general process would be the same but some details would differ.

First, the Chinese nationals would have to indicate to their Government that they wished their blocked balances released. It might be found desirable to give private persons only local currencies in exchange for blocked foreign balances. How important this restriction would be is uncertain since they could later buy any currency desired. The Chinese Government would then make the arrangements with the Fund, after which the Chinese Government would transfer to its nationals the money which the Fund puts at China's disposal in exchange for their sterling balances. Title to the sterling balances would be transferred to the Fund.

So long as China is willing to take yuan for the blocked sterling, the Fund would supply it, if necessary buying or borrowing yuan for the purpose. If, however, China's Treasury asks for United States dollars or Brazilian milreis, the Fund might wish to satisfy itself first that China needed those currencies for "legitimate" purposes.

The Treasury of China would be permitting its nationals to avoid the risk of exchange that holders of blocked sterling would otherwise have to bear. Forty percent of that risk would be borne by the Treasury of China since it would be committed to repurchase 40 percent of the sterling unblocked to it; forty percent would be borne by the British Treasury for a similar reason. The Fund would accept the other 20 percent of the exchange risk.

The Treasury of China might impose a two or three percent charge on its nationals for the transaction. That would help cover the service charge imposed by the Fund, and leave a small profit after expense of administration.

Consideration might be given to the possibility that a small annual charge could be imposed by the Fund on the blocked balances it held. In the above illustration, for example, a charge of 1 percent a year could be placed on both China and England on the blocked sterling not yet repurchased.

Arrangements for the transaction might take some time, but for the individual holder of the blocked balance the transaction would be simple. After the initial arrangements had been completed, the transactions between the Fund and the two Governments involved would assume an almost routine character. Careful watching of the balance of payments of the various countries concerned in the transactions would be necessary continuously. That task, however, would be one of the important current responsibilities of the Fund's technical staff at all times and with all countries. The condition and movements of the international accounts of the member countries would be to the Fund's research staff, what the thermometer, stethoscope, x-ray, and microscope, etc., are to the diagnostician. Without a carefully drawn up and compiled quarterly balance of payments account of member countries the technical staff of the Fund would be greatly handicapped in their recommendation of decisions and policies. With adequate data in their hands they would be in a position to know and understand what was going on in matters pertinent to the work of the Fund.

How much could the Fund be expected to do with blocked balances? The sum of blocked balances which the Fund would be called upon to purchase might be greater than the Fund felt it could afford to take. If, for example, it were asked to absorb two billion dollars of blocked balances it might well hesitate if such assets were not to be liquid. It might be three years before they could sell any of it, and even then they might not be able to sell it at a rate faster than 4 percent a year. The Fund could, it is true, invest the assets in interest-bearing Government obligations (of the country in which the currency is blocked), but they could not convert those into gold or other currencies without either risking a loss on the transaction or adding to the possible drain of gold from the country whose obligations they were selling.

If the Fund attempted to sell a substantial amount of (say) British Government obligations payable in sterling to residents of United States, the price the Fund would get might be substantially less than what the Fund paid for the bonds.

Moreover, if the Fund invested the blocked sterling in British Government bonds, and then sold them in New York, and later the Americans sold the bonds in London getting sterling which would not be blocked, the end result would be that England would be subjected to the drain on her foreign exchange resources which she wished in the first place to avoid. It seems, therefore, that if the Fund is to be permitted to invest its sterling in British Government obligations, it should not be permitted to sell them except as England repurchased them according to the schedule, or unless the British Government approved the sale.

Yet the Fund would like to take over as much of the blocked balances as possible, but, on the other hand, could not tie up too much of her liquid resources in frozen currencies. A way out of the dilemma might be to permit the Fund to borrow in New York (or anywhere else except England) using as collateral the British Government bonds. With that possibility for converting a frozen asset into a liquid resource the Fund could afford to take more blocked balances. It might even be feasible to arrange that the bonds be special ones payable in either gold or sterling (at the holder's will), in order to increase their collateral value. Since 40 percent of the blocked sterling the Fund acquires would have to be repurchased with gold anyway, this latter possibility might be acceptable to the Government concerned.

The end result of the exercise of this authority should be:

1. Private holders of blocked sterling balances should be able to convert them at once into their local currencies by selling them to their Government. With that currency nationals, as distinct from the Government, could purchase any currency they wished.
2. Their Government would be in possession of sterling which at small risk of exchange on 40 percent of its purchases it could sell to the Fund for any currency it wished.
3. England could at once remove restrictions on the withdrawal of foreign-owned sterling balances without fearing any serious drain on her gold or other foreign exchange assets. She would have to purchase back only 40 percent of the funds withdrawn under this authority at the rate of 2 percent a year, beginning after three years.

Two gains would quickly emerge: one, the demand for withdrawal would be greatly lessened by the fact that foreign holders would have no reason to hurry their withdrawal, and two, the post-war pressure against sterling would be dissipated and hence the sterling rate could be more easily maintained.

If adjustment of the price of sterling in terms of other currencies were later justified by a basic unbalance, then only 40 percent of the resultant exchange loss would be borne by England, and not more than 40 percent by the country having blocked balances, and 20 percent by the Fund.

4. Finally, foreign purchasing power would be released to be spent wherever desired, and one of the potent obstacles to a return to fair trade practices removed.

This provision on blocked balances is not proposed as a method of freeing balances which might accumulate after the war. Unless the funds to which this particular power are to apply is clearly delimited, the provision would overlap and largely nullify other provisions contained in the proposal specifically designed to meet current and developing situations in a country's balance of payments. The provision described in the previous several pages is not intended to make it possible for owners of foreign balances—whatever the source of these balances may be—to withdraw those balances at will at the expense of the Fund's assets. It is hoped that the Fund will make it possible for all countries to remove restrictions on exchange transactions, but this particular provision should be used as the vehicle to free only the blocked balances in existence at the date the country joins the Fund. It is for the purpose of clearing up the present bad situation with respect to blocked currencies that this provision is included.

In the event a similar situation develops in the future, authority is granted to the Fund provided four-fifths of the member votes approve to initiate a similar program which would apply to the then-existing balances.

To provide the data necessary for the operation of this provision each member country should be required to file with the Fund a record of the balances in its country owned by residents of foreign countries, and also a record of the balances of its nationals held abroad. These balances should be broken down in the significant categories as required by the Fund. A quarterly report should be filed keeping the information up to date.

The fact that each of the parties concerned, i.e. the country in which the balances are blocked, the country whose nationals own the balances, and the Fund—will be undertaking an exchange risk should help prevent undesirable practices or misapplication of this provision.

In evaluating the effectiveness of this provision to liberate blocked balances, it must be borne in mind that the mere existence of this power will remove much of the eagerness to withdraw funds in the near future. That reaction would in turn make it easier for England (and other countries) to remove exchange restrictions. Even though the blocked balances in various countries outside of the United States were as high as the equivalent of 6 billion dollars, only a portion of this amount would be involved unless there were strong fears of depreciation of sterling—a development the Fund could do much to prevent. The greater the assurance that foreign exchange rates will be stable, and the knowledge that large portions of the funds will be unblocked periodically would encourage holders of these balances to diminish their withdrawal requests.

However, since the amount that the Fund might be called upon to absorb might be larger than it wished to handle at the beginning, the Fund is given the authority to set a maximum percentage of blocked balances that could be handled through this provision in any given period. It would be easy enough to adjust that percentage upward if circumstances indicated it could be safely done.

The fixing of rates.

The Fund would fix the rates at which it would exchange a member's currency for another, and the rates at which it would buy and sell gold in exchange for local currency.

The guiding principle in the fixing of such rates should be stability in exchange relationships. To assure the maximum stability in rates, it is suggested that alterations in rates set by the Fund beyond the range of narrow fluctuations applying to all rates be permitted only with the consent of four-fifths of the member votes. If a country does not wish to accept or pay the rate fixed by the Fund, it can, of course, attempt to complete its transactions through other channels. Nonetheless the authority to set the rates of exchange at which the Fund is willing to operate can be an important and in some cases a decisive influence on the rate at which transactions are made outside of the Fund.

The service charge for exchange transactions should be no larger than necessary to cover the direct costs of the operations.

Borrowing from the Fund.

Any member country can borrow its local currency from the Fund for one year or less up to 75 percent of the currency of that country held by the Fund, provided such loan is approved by three-fourths of the member votes.

A country borrowing such funds shall pay to the Fund an interest rate of 1 percent a year. Revenue from such loans shall constitute a reserve for the Fund which can be drawn upon to meet expenses or losses of the Fund.

The object of the provision permitting any member country to borrow local currency from the Fund for one year or less up to 75 percent of the currency of that country held by the Fund, provided such loan is approved by three-fourths of the member votes, is to make it possible for a member country to reduce the burden of participation on its budget. Some of the countries may at times be confronted with deficits, and the investment that they would have in the Fund should be a source to which they could turn in time of need to borrow at very low rates of interest. It may well prove to be the case that every country operating at a deficit would prefer to borrow up to the maximum of its local currency, at 1 percent, rather than go into the market and possibly pay 2 or more percent. Inasmuch as a fund could, if necessary, always obtain such local currency by rediscounting the paper in that market, there would seem to be no reason why the Fund should object to such practice on the part of those countries wishing to avail themselves of the low rate of interest. Also, from the Fund's point of view, it would be desirable to permit such loans since it would prove a source of revenue with which to meet expenses or losses of the Fund.

Borrowing by the Fund.

It is suggested that the Fund should have authority to borrow at such rates as the Fund may recommend, the currency of any country, provided four-fifths of the member votes approve the terms, amount and conditions of such borrowing.

This provision gives the Fund power to obtain any currency it may feel it will need only for a short time. It also makes it possible for the Fund to expand its resources to meet short-term special demands.

Currency sold to a government in default.

No sale of any currency from the Fund should be made to a member without approval of four-fifths of the member votes when the sale of such currency so sold is to make possible adjustment of a government foreign debt which had been defaulted. This provision is probably necessary in order to prevent utilizing the Fund for the purpose of servicing a foreign debt. The resources of the Fund should be used for such purpose only when most of the Board feels that the borrowing for debt adjustment is temporary, or when they are satisfied that basic adjustments are being undertaken.

Accept deposits, act as clearing house for international movements of funds, balances, checks, etc.

The power to accept deposits and perform clearing functions would enable the Fund to operate more efficiently in its foreign exchange operations. It is not intended that the Fund shall perform banking functions other than those supplementary to the task of foreign exchange stabilization.

Deal only with (a) the Treasuries of the participating countries, or with the official stabilization funds of those countries, and (b) with the bank designated by the participating government as its fiscal agent, and (c) with international banks and international corporations owned by at least five governments.

The Fund is envisaged as an intergovernmental agency which should interfere as little as possible with the operations of private banks, brokers and dealers. It is only when the supply-demand relationship of exchange arising out of usual transactions through the customary channels are causing pressure in an undesired direction, that the Fund begins to operate.

The Fund will also wish to deal with any intergovernmental financial institutions such as the proposed Inter-American Bank. The Fund shall have the authority to invest any currency it holds in "short-term" securities—commercial or government—of the country of that currency provided a four-fifths vote of the member votes shall approve and provided further that the approving votes shall include those of the country in which the investment is to be made.

The Fund shall also have authority to sell the obligation it holds of the member countries provided four-fifths of the member votes approve, and provided the representative of the country in which the securities are to be sold approves.

Value of total holdings should remain unchanged.

No change in the gold value of any currency of the participating countries shall be permitted to alter the gold value of the total currency holdings of the Fund. Through the day-to-day operations of the Fund, the proportion of various local currencies held by the Fund will constantly change, but the book value of the total assets would remain the same in terms of the unit of account (presuming the small service charges and interest revenue would cover operating expenses). The unit of account used should either be gold or a new international unit defined in terms of gold. If the currency of any of the participating countries should depreciate, that country must deliver to the Fund an amount of its local currency equal to the decrease in the value of that currency held by the Fund. Likewise, if the currency of a particular country should increase, the Fund must deliver to that country an amount (in the currency of that country) equal to the resultant increase in the gold value of the Fund's holdings.

An exception to the above would be the blocked balances purchased by the Fund under provision described earlier. Those currencies could be kept in a separate account until repurchased or sold. The only portion upon which there might be a loss is in the 20 percent portion, the exchange risk on which is borne by the Fund. The sole justification for placing that exchange risk on the Fund is the desire to spread some of the risk of sterling accumulations resulting from the war on all nations benefiting by the successful outcome. If that is not considered adequate justification, the Fund can be relieved of any risk.

The only serious bookkeeping loss that could be experienced would be in the event the unit of account—either a new international unit fixed in terms of gold or the dollar having a fixed gold content—were to appreciate in terms of all or most of the currencies. That is equivalent to saying that all other currencies depreciated in terms of the unit of account. There is no way to avoid that possibility unless the unit of account were defined in terms of an index of other currencies—a complicated device and of doubtful utility.

A country failing to contribute to the Fund sums due the Fund shall be dropped as a member, provided a majority of the member votes so decide. Any member dropped shall have returned to it an amount (in its own currency) equal to its contribution minus any sum due by that country to the Fund.

III. Eligibility for Membership

The conditions selected to be fulfilled before any country can be eligible for membership in the Fund constitute an important part of the plan. It will also prove to be one of the most disputed parts. Serious differences of opinion as to the wisdom of including many of the conditions listed are certain to exist. It will be said of some of them that they embrace far too wide an area of economic policy. Others on the list will be opposed on the grounds that they involve policy decisions which cannot be shared by or delegated to any combination of nations. And against some of the conditions listed opposition will arise because there will be differing views as to the economic soundness of some of the requirements, and of the political feasibility of others. Finally, some of the requirements for eligibility listed may be very difficult for many countries to accept because acceptance would involve abandonment, or rather suspension, during period of membership, of certain legislative powers. Nonetheless, the list is submitted because the chief purpose of this memorandum is to suggest possibilities and stimulate discussion.

It is vital to the success of any international stabilization fund designed to play a really useful role that there be a suspension of certain economic elements of national sovereignty in favor of international collaboration. It is well to recognize at the outset that unless there is willingness to keep dormant, for a trial period at least, certain rights to unilateral economic action which directly affect other countries, there is no hope that any international instrument can be devised to help bring about the kind of collaboration among nations essential to a prosperous and peaceful world. If no government is prepared to sacrifice for the sake of a larger though possibly a less obvious good what it regards as an advantage when that advantage is obtained at the expense of some friendly power, then the world will revert to the barbaric international economic relationships of the 'twenties and 'thirties.

The strength of the position of those who call for the temporary transfer to an international body of certain sovereign economic powers rests in the conviction that the long-run interests of most countries are best served when no country seeks to gain at the expense of another. It is true that rich and powerful countries can for long periods safely and easily ignore the interests of poorer or weaker neighbors or competitors, but by doing so they will imperil the future and reduce the potentiality of their own level of prosperity. The lesson that must be learned is that prosperous neighbors are the best neighbors; that a higher standard of living in one country begets higher standards in others, and that a high level of trade and business is most easily attained when generously and widely shared.

It is with these thoughts in mind that the following list of conditions for eligibility should be examined.

Any member of the United or Associated Nations is eligible for membership in the Fund provided it agrees:

To abandon, not later than one year after joining the Fund, all restrictions and controls over foreign exchange transactions with member countries, except with the approval of the Fund.

It is important that participating countries be motivated by common objectives in conceiving their foreign exchange policies and desirous of adopting basically harmonious procedures in implementing such policies. Some allowance will, of course, have to be made for reasonable differences because of dissimilarities in the economies of various countries, and early in the Fund's existence there would need to be toleration of lack of uniformity in policy. In general, however, and as basic and long-run prerequisites to participation, it would seem necessary for each member country to subscribe to the general policies of permitting foreign exchange trading in an open, free and legal market, and to abandon, as rapidly as conditions permit, all restrictions or controls by which various classes of foreign exchange transactions have been prohibited or interfered with, other than from consummation in such a free market.

This requirement calls for careful examination. There has been too easy an acceptance of the view that an enlightened trade and monetary policy requires complete abandonment of controls over international economic transactions. There is a tendency to regard foreign exchange controls, or any interference with the free movement of funds and of goods as, ipso facto, bad. This view is both unrealistic and unsound. It ignores the fact that there are situations in which many countries frequently find themselves, and which all countries occasionally meet, that make inevitable the adoption of controls of one character or another. There are times when it is in the best economic interests of a country to impose restrictions on movements of capital, and on movements of goods. There are periods in a country's history when failure to impose exchange controls, or import or export controls, have led to serious economic and political disruption.

It probably would be fatal to the Fund if the conditions of participation in it were based upon the assumption that no restrictions upon exchange or upon trade were permissible.

It would be equally unfortunate, however, if it were to be assumed that restrictions on foreign exchange transactions, on the international movement of goods, and the use of multiple currency devices were desirable instruments to employ under all circumstances for safeguarding or controlling international economic relationships. It is as easy to exaggerate the need for such instruments and the benefits derived from the use thereof, as it is to exaggerate their adverse effects.

The theoretical bases for the belief still so widely held, that interference with trade and with capital and gold movements, etc., are harmful, are hangovers from a Nineteenth Century economic creed, which held that international economic adjustments, if left alone, would work themselves out toward an "equilibrium" with a minimum of harm to world trade and prosperity.

It is doubtful whether that belief was ever sound. Certainly few competent students of international economic affairs would hold that it applied to present conditions or to conditions likely to prevail during the post-war period. The forces of adjustment set into motion by changing trade balances, flows of gold or of purchasing power, changes in price levels and all the phenomena that the expert in the subject recognizes as instrumentalities in the so-called mechanism of adjustment of international balances of payment, rarely, if ever, work out quickly enough or effectively enough to be depended upon to achieve good results. In fact, it is doubtful if they ever were depended upon, unaided, to bring about the desired "equilibrium". In modern times, particularly, there has always been somewhere in the picture some measure of control over, some measure of interference with the movement of funds and goods in order to bring about certain desired ends.

The task before us is not to prohibit instruments of control but to develop those measures of control, those policies of administering such control, as will be the most effective in obtaining the objectives of world-wide sustained prosperity. To cast aside certain effective instrumentalities of control because they may be and have been abused, is just as foolish as it would be to rely solely on the self-interest motive of individuals as a means of solving our economic problems.

The requirement suggested above that there be accepted the general policy of foreign exchange trading in open, free and legal markets, and the abandonment as rapidly as conditions permit of restrictions on exchange controls, should be taken to mean that there shall be acceptance of the principle that controls and restrictions will be employed only when they are clearly justified by the economic circumstances, and only to the extent necessary to carry out a purpose contributing to general prosperity. The chief difficulty in the application of the principle will be agreement as to what is in the interests of general prosperity. The danger of conflicting policies lies not only in the difficulty of distinguishing between real and specious advantage, i.e. between the advantages of a special group as against the advantages of the whole—but much more in the difficulty of reconciling short-run interests with long-run interests. One of the purposes of this Fund is to provide for a more reasonable basis for such distinction, and to supply the means through which it should be possible to pursue long-run and broader interests, without too great a sacrifice of the narrower and short-run interests.

The second requirement or condition for participation should be the acceptance of the principle that no participating country will alter its exchange rate on currencies of other countries without the consent of the Fund.

This condition is very important. Its obvious purpose is to eliminate the possibility of competitive depreciation of currencies. It recognizes that there are occasions when it may be economically wise for a country to increase or decrease the value of its currency in terms of other currencies. When a country's balance of payments is in disequilibrium for causes that do not appear to be temporary, and if that disequilibrium uncorrected will deplete a country's foreign exchange reserve, then altering the value of that currency in terms of other currencies is one of the ways in which the disequilibrium could be corrected. Other ways of correcting disequilibrium in the balance of payments are the imposition of restrictions on imports and subsidy of exports, either directly through import and export controls, or through use of exchange controls or multiple currencies. Which method or methods are best suited to accomplish the objective depends on the cause of the disequilibrium, the circumstances, the country, and the time.

The circumstances under which it may be wise to alter an exchange rate in order to correct maladjustments of the balance of payments have long been a matter of controversy among monetary theorists. But there is general agreement that an alteration in the value of a currency in terms of gold (or in terms of important currencies) is a very serious business and one not to be undertaken lightly. The change in the value of a currency in terms of gold or other currencies means that a change has by that act been imposed on the other currencies. When, for example, the dollar changes in terms of sterling, obviously sterling changes in terms of the dollar. Because all countries are to a lesser or greater degree affected by the action of any one country with respect to the value of its currency, it is only reasonable to demand that such action should not be undertaken without careful—and, if possible, impartial—weighing of the consequences of the action on other countries.

The purpose of requiring approval by the Fund as a condition of alteration of currency is to assure joint consideration of the merits of the proposed action and thereby avoid unilateral action taken to obtain presumed competitive short-run advantages irrespective of the consequences of the impact of the step on other countries or even on the same country. The mere fact that membership would be forfeited if a country acted in so important a matter contrary to the wishes of the majority would make countries hesitate to undertake lightly a change in their currency. The very discussion of the problem by competent representatives of various countries should in itself be a potent influence to avoid unnecessary changes. It would, moreover, be an assurance that when a change is made it would not be a signal for numerous other countries to follow in their own real or presumed interest.

There will be difficulties surrounding the operation of this condition, the most important of which would be the necessity for secrecy when a country is contemplating a step such as altering the value of its currency in terms of other currencies. If a country believes that it should depreciate its currency relative to others, it could hardly throw that matter open for public discussion. By so doing it would stimulate speculative activities in the exchange market which might have the effect of precipitating the very action being considered. Some procedure would have to be devised to make possible deliberations without publicity. It might be that an Executive Committee could undertake to pass on such cases, or it might be possible to arrange that during such discussions no country will accept or permit movements of capital to and from a country considering the step.

Some objection to this requirement will doubtless be raised on the ground that such a provision means that other countries pass judgment on what is a domestic monetary matter. The necessity for obtaining approval of other countries on such a matter will be regarded in some quarters as a serious infringement of sovereignty. There is some measure of truth in this but hardly enough to constitute a decisive reason for not participating in the Fund. Alteration of a currency affects other countries as well as the country making the change. It is, therefore, only reasonable to demand that the other countries have some say in the decision. Furthermore, all members would be surrendering their "rights" to an equal extent. Unless nations are willing to sacrifice some of their power to take unilateral action in matters of international economic relations, there is very little hope of any significant international cooperation—let alone collaboration.

To avoid giving richer nations greater authority on such matters, by virtue of their larger number of votes, it may be desirable to give each participant only one vote when questions of altering currency rates are being voted upon. As a last resort, a country always has the choice of withdrawing from the Fund so that it can always preserve its sovereignty in monetary matters if it feels it is being prevented by the Fund from taking action deemed important to its own interest.

The principle worked only tolerably well in the Tripartite Accord during 1935, 1936 and 1937, and better machinery for more adequate discussion and greater willingness to recognize the legitimate interests of other countries, needs to be developed to achieve best results. In evaluating the need for collaboration on questions of foreign exchange rates, it is well to remember that unilateral action can easily be neutralized by similar action on the part of other countries. When a competitive advantage is sought it is essential if it is to be successful that other countries do not take similar action. Otherwise the advantage hoped for is lost. Where the chief objective sought is not a competitive trade advantage in the international market but modification of the domestic price structure or money market, the favorable effects cannot be wholly negated by action of other countries. Since, however, the chief reason for establishing the requirement is to avoid competitive depreciation of currencies, the fact that unilateral action can be easily neutralized constitutes an important argument for securing approval of the Fund before taking such action.

Each country agrees (a) not to accept or permit deposits or investments from any member country except with the permission of that country, and (b) to make available to the government of any member country at its request all property in form of deposits, investments, securities, of the nationals of member countries, under such terms and conditions as will not impose an unreasonable burden on the country of whom the request is made.

This is a far-reaching and important requirement. Its acceptance would go a long way toward solving one of the very troublesome problems in international economic relations, and would remove one of the most potent disturbing factors of monetary stability. Flights of capital, motivated either by prospect of speculative exchange gain, or desire to avoid inflation, or evade taxes or influence legislation, frequently take place especially during disturbed periods. Almost every country, at one time or another, exercises control over the inflow and outflow of investments, but without the cooperation of other countries such control is difficult, expensive, and subject to considerable evasion.

It would seem to be an important step in the direction of world stability if a member government could obtain the full cooperation of other member governments in the control of capital flows. For example, after the war a number of countries could request the United States not to permit increases in the deposits or holdings of their nationals, or to do so only with a license granted by the government making the request. Or, some countries greatly in need of capital might request the United States to supplement their efforts to attract capital back to the native country by providing information, or imposing special regulations or even special taxes, on certain types of holdings of the nationals of the foreign countries.

The search for speculative exchange gains or desire to evade the impact of new taxes or burdens of social legislation have been one of the chief causes of foreign exchange disturbances. Less hectic and less dramatic yet in the case of some countries during some stages of their development capable in the long run of even greater harm, is the steady drain of capital from a country that needs the capital but is unable for one reason or another to offer sufficient monetary return to keep its capital at home. The assumption that capital serves a country best by flowing to countries which offer most attractive terms is valid only under circumstances that are not always present.

A good case could be made for the thesis that a government should have the power to control the influx and efflux of capital, just as it has the authority to control the inflow and outflow of goods and of gold. In fact, virtually every participating government has already practiced these controls to some extent during this war. The consequence of cooperation in this matter among the member governments would give each government much greater measure of control in carrying out its monetary and tax policies. Such an increase in the effectiveness of control means, however, less freedom for owners of liquid capital. It would constitute another restriction on the property rights of the 5 or 10 percent of persons in foreign countries who have enough wealth or income to keep or invest some of it abroad, but a restriction that presumably would be exercised in the interests of the people—at least so far as the government is competent to judge that interest.

The inclusion of this provision does not mean that capital flows between foreign countries would disappear or even greatly subside; it means only that they would not be permitted to operate against what the government deemed to be the interests of any country.

A fourth condition might be that each country agrees not to enter upon any bilateral clearing arrangements except with non-member countries, and then only with the consent of the Fund, and to establish no geographically preferential exchange rates.

The justification for setting up this requirement for participation is to eliminate discriminatory practices in foreign trade which result in friction, unfair competition, retaliation, and sharp trade policies which serve to disrupt good economic and political relations. It means that for the sake of the larger good to be obtained countries agree to give up opportunities for making certain advantageous arrangements. If each country is to operate in accordance with its own immediate interest, irrespective of long-run effects and irrespective of the impact of its actions on other countries, a repetition of the pre-war chaotic conditions in trade will result and again threaten political and economic stability of other nations. The task which confronts the high officials of all nations is to make possible a high level of business activity and of foreign trade within the framework of reasonable and fair foreign trade practices. Just as individuals subscribe to a government of law to obtain maximum prosperity and effectiveness for the whole group, even though adherence to that law involves restrictions on individual behavior at numerous points, so must nations give up lesser advantages for greater good. The concept of sacrificing some immediate benefits for the sake of larger good is the foundation stone of peace and economic collaboration among nations, just as it is the keystone of peace and prosperity within a nation.

The operations of the two agencies discussed in this report should help considerably to remove the justification for trade practices adopted to protect or strengthen an exchange position.

There are times when gains could accrue from bilateral clearing arrangements without significant adverse effects on other countries, but in general the operation of the Fund should have the effect of making such clearing arrangements much less profitable as among members of the Fund. One of the specific objectives of the Fund is to make available for each member a supply of foreign exchange adequate to enable it to operate more freely and with a higher level of trade than would otherwise be the case. Nevertheless, in the interest of flexibility, and to take care of those situations in which circumstances may warrant a bilateral clearing arrangement, it should be possible for a country to enter upon such an arrangement provided it can obtain the Fund's approval. Discussions by the Fund of such proposals do not require the secrecy or the speed involved in consideration of alterations of exchange rate, and discussions of the advantages and disadvantages of the particular proposal should prove beneficial. An objective decision on the economic wisdom of such proposal is more likely to emerge from the discussion by the appropriate committee of the Fund than from the consideration by one or two countries alone where vested or political interests are likely to dominate the decision.

A fifth requisite for membership might be subscription to the principle that no monetary or banking or price measure or policy would be adopted, the effect of which, in the opinion of a majority of the member votes, would be to bring about sooner or later a serious disequilibrium in the balance of payments, if four-fifths of the member votes of the Fund submitted to the country in question their disapproval of the adoption of the measure.

This provision would prove to be more troublesome than any of the others and yet it would seem to be important to the successful functioning of the Stabilization Fund. Serious inflation or deflation in any one country would affect not only exchange rates and trade, but price levels in other countries as well. It is impossible for any country to take action of that character which does not have important effects on other countries with whom it competes or with whom it carries on trade. The decision as to whether a particular measure or policy contemplated would bring about a serious disequilibrium in the balance of payments would be a difficult one on which to get agreement. To estimate even very roughly the quantitative effects of any given measure on a country's balance of payments is a very difficult task at best. After sufficient agreement was reached on that point it would be even more difficult in many cases to get any measure of agreement as to whether the adoption of the measure in question was economically wise or not.

There are times when domestic consequences are sought which are more important to a country than the adverse effects that might follow in some directions from the accompanying disequilibrium in the balance of payments. There are other instances in which disequilibrium provides a necessary corrective, and frequently a country is confronted with only poor choices and disequilibrium is the least undesirable of them.

To assume that it would ever prove easy to get four-fifths of the member votes to take so drastic a step as to disapprove a measure proposed by a sovereign government deemed by it to be in its own interest, is to ignore the known complexities of the monetary problems, and the political realities of international relationships.

Notwithstanding the difficulties involved in exercise of a veto power by the Fund over monetary measures, there will be instances in which the case is clear enough and the consequences important enough to justify the exercise of that power. It is assumed that the Fund would not concern itself with minor measures. To help avoid the error of attempting to evaluate measures which are not important, the requirement provides that a majority of the members would have to be of the opinion that the results of any given measure are likely to be serious. It then requires four-fifths of the member votes to authorize official disapproval. It may well be that despite this degree of protection against arbitrary action or needless interference most countries would object to subjecting what they believe to be purely domestic affairs to international supervision. If compromise with this view is found feasible, it is hoped that it takes the form of requiring a larger majority—say 90 percent instead of 80 percent of the member votes, or, as a last resort, requiring that the disapproval of the Fund call forth the promise of the offending country to reexamine her position in the light of the Fund's report.

In any case, the discussion which would take place by an international committee of the character envisaged—men expert in their fields, international in their outlook, and scientific in their approach—could not help but prove very salutary. The educational process to which officials, administrative and legislative, in each country would be subjected in defending specific policies or measures before such a committee would in itself go a long way toward improving the quality of monetary, credit and banking policy. It probably would be necessary for the committee, certainly during the early years, to be very tolerant of policies pursued by participating countries. Gradually, however, there should develop a greater reluctance on the part of member countries to take measures which do not meet the approval of the majority of the members of the Fund. The success of the Fund in this field would depend in large measure upon the wisdom with which matters of this kind are examined and the degree of sympathetic understanding the Fund was capable of displaying.

The member countries agree (a) to embark within a year after joining upon a program of gradual reduction of existing trade barriers—import duties, import quotas, administrative devices—and further agree (b) not to adopt any increase in tariff schedules, or other devices having as their purposes higher obstacles to imports, without giving reasonable opportunity for the Fund to study the effects of the contemplated change on exchange rates and to register its opinion. In rendering an opinion the Fund will make recommendations to which member governments agree to give serious consideration.

It might contribute notably to conditions tending to promote exchange stability if participating countries, particularly those with large reserve of foreign exchange, were to agree to a gradual reduction of duties on imports. It might be possible to devise an acceptable formula for general and gradual tariff reduction to a level more in harmony than were tariff policies of the twentieth century with the objectives of reducing the causes for international friction and increasing the standard of living the world over. Those high tariff policies in the main reflect adherence to the traditional, crude, mercantilist fallacies. So widely held are those fallacies, so persistently clung to by persons who should know better, so potent are they in shaping many aspects of domestic and foreign policy, and so unfortunate in their effects on world peace and prosperity, that one is tempted to list "mercantilism" or its more expressive heir "protectionism" as "World Enemy No. 1," in the economic sphere.

Yet, though there is no doubt as to the evils of crude protectionist policies, caution must be exercised in attempting to translate a policy of lower tariff schedules into an actual program. There is danger of retarding progress by advocating a trade policy which ignores the sound basis for the existence of some import duties. There is too easy an assumption that as much reduction as possible in all duties is desirable; that any movement toward free trade is, ipso facto, a good thing for the world.

In the reaction against the crude protectionist fallacies that a country with high standards of living must adhere to a policy of high tariff schedules if it is to prevent widespread unemployment or deterioration of its high standard of living, there is an inclination to throw the baby out with the bath and assume that all duties are bad; that free trade, or rather tariff for revenue only, is the ideal toward which all enlightened nations should move as rapidly as possible.

The belief that reduction in all import duties increases trade and yields a higher standard of living for all countries under all circumstances and in all stages of their economic evolution assumes that countries are usually utilizing virtually all their capital and labor; that a country chiefly agricultural in its economy has as many economic, political and social advantages as a country whose economy is chiefly industrial, or as a country which has a balanced economy; that there are no gains to be achieved by great diversification of output. These assumptions, essential to the belief that "Free Trade" policy is ideal, are not valid. They are unreal and unsound. "Free Trade" policy grossly underestimates the extent to which a country can virtually lift itself by its bootstraps in one generation from a lower to a higher standard of living, from a backward agricultural to an advanced industrialized country, provided always it is willing to pay the price. The view further overlooks the very important fact that political relationships among countries being what they are, vital considerations exist in the shaping of the economic structure of a country other than that of producing goods with the least labor.

The subject of the best tariff policy for a given country at a given period in its history is a most interesting one, but justice could not be done to it in the space that could reasonably be allocated to it here. A great deal has been written on the subject and the interested reader in his search for sound policy will find that the complexity of the problem is apt to increase with the profundity of his reading. Yet one conclusion is certain to emerge from his study of the subject, namely, that most import duties are too high, that many duties remain too long, that few are imposed for sound reasons, and almost none of them are reevaluated often enough by the law-making bodies in the light of changing needs and conditions.

The value of requiring participating governments to agree to a general policy of lower tariffs lies solely in the recognition that most duties in the tariff schedules of every country, at their present level, are inexcusable on any economic, political or social grounds. Their existence merely reflects uncritical adhesion to protectionist policies or the successful pressure of some powerful vested interest, or both. It is to place on the defensive obstructions to trade, whether in the form of unreasonably high duties or in any other form, that commitment to lower tariff policies might be justified.

Yet, it cannot be overlooked that the shaping of tariff policy has been for too long the prerogative of lawmaking bodies and the battleground of legislative maneuvering to expect the Congresses and Parliaments to subordinate to an international body their authority on such matters. If the sugar, wool, wheat growers of the United States, and the shoe and textile, pottery, and steel manufacturers—to name only a few of the industries insisting on high protective duties—were to see in any suggested agency a definite threat to what they regard as necessary protection to their industry, they would combine and probably rally enough support to their crusade to ruin the prospects of acceptance by Congress of any proposal no matter how attractive the scheme might be to economists, statesmen, foreign trade associations, college professors and bankers.

It would seem to be a far wiser policy not to attempt too much and thereby jeopardize any but an innocuous program. On this issue, as on no other, prudence dictates compromise. The most one can hope to get is adherence to a principle without surrender of any authority. Hence the requirement calls only for public adherence to the stated principle, and permission to the Fund to submit a report giving reasons for its disapproval of an added barrier to trade if the Fund deems it harmful. If any international agency or organization wrings more than that out of the American and other publics, a miracle in economic morality will have been wrought by this war.

Another possible condition of participation that merits attention is the agreement that no Government or Central Bank shall default on its external obligations, or any part thereof, without consent of the Fund.

This requirement has considerable possibilities for good. If the flow of private capital from capital-rich to capital-poor countries is to be stimulated and the flow of specialized capital among countries is to be fostered, something drastic must be done to reestablish confidence of private investors in the integrity of foreign borrowers. Defaults by governments and states have been in the past too easy a way out of foreign exchange and budgetary difficulties. The defaulting country frequently experiences an immediate gain but unfortunately the long-run losses have far more than outweighed the gains. If the Fund and the Bank could be a potent force for preventing defaults (as well as keeping interest rates reasonably low), a long step forward will have been made toward the increased productiveness of all countries.

It can hardly be expected that objective decisions on defaults can be made by the defaulting country or by the country gaining most by continued servicing of a debt. To make what takes on the character of compulsory arbitration in debt adjustment an acceptable and workable instrument, the proposed judgment must be that of a large group of nations, the majority of whom are not directly and immediately affected by the decision. Consideration of the pros and cons of a contemplated default by the Fund would seem to promise that kind of objectivity, and therefore not be a requirement that would stand in the way of acceptance by any government.

Not to subsidize—directly or indirectly—the exportation of any commodity or service to member countries without consent of the Fund.

One of the unfair trade practices frequently resorted to in the past has been export subsidies. Most countries have been guilty of subsidizing some exports either by direct or indirect methods. It is easy for the practice to grow as there are in every country powerful interests who because of a monopoly position or political influence, at the expense of the public, are able to keep up the price of a product at home by practicing subsidized dumping on foreign markets. This device in essence is no different from the use of multiple currencies or special clearing arrangements except that the gain in the latter case is shared by more persons. They all aim to undersell a foreign competitor not by offering the same goods at a lower price, or better goods at the same price, but by undercutting a foreign competitor at the expense of the taxpayer of the exporting country.

It is just such practices that give rise to rivalries which constitute fertile soil for international friction. If subsidies to exports are condoned there is no logical justification for objecting to any kind of trade device designed to increase exports or decrease imports. The result would be a repetition of the ruthless fight for foreign markets that characterized international trade in the pre-war decade.

It might be possible to obtain acquiescence among the member countries not to resort to the more obvious forms of subsidies without consent of the Fund. Since the Fund would be a sort of court of appeal, the possibility of subsidizing the export of a commodity or service exists. Yet presumably it would be invoked only under special circumstances. The fact that approval of the Fund were necessary would be helpful to governments in their struggle against vested groups seeking special advantages. Though it will be found very difficult to get a satisfactory working definition of an indirect subsidy, it should be at least possible to define the term so as to apply to the more obvious devices.

The Fund would probably have to permit subsidies to shipping and air travel. Almost every country subsidizes these two for military reasons, for economic reasons, and reasons of national prestige. It is irrelevant that much of the defense for ship-building and shipping based on economic and patriotic grounds is specious. These subsidies are so deeply imbedded in custom and policy that it is useless to attempt to modify them through an agency such as we are discussing.

Subsidies to tourists, to student voyages, etc., are of a different character. It may well be in the interests of all countries, and certainly is in the interests of some countries, to attract tourists by subsidies of one form or another. This subsidizing of exports of services seems to arouse little objection in the importing country (i.e. in the countries whose nationals do the touring) and can at least be defended on social and cultural grounds. Since United States is probably the most generous producer of profitable tourists, there is an added justification for attracting Americans abroad by subsidies if necessary, namely it will help the United States to develop a much desired "unfavorable" balance of payments through the most desirable available channels.

All considered it were probably better to exclude "services" altogether from the prohibition of subsidies, and save the Fund much trouble. It would, moreover, make it less unlikely that the requirement would find acceptance by enough nations.

It may be properly questioned whether an agency of this character is the appropriate instrument for obtaining fair trade practices in foreign trade. It might be that some other agency like a league of nations should be the vehicle, or possibly dependence should be on a program of multilateral treaties. However, it does seem that it should be less difficult to obtain agreement on such matters when the vehicle is an agency, membership in which has obvious economic advantages. Moreover, a country could feel it could always withdraw from the Fund if it deems its interests significantly harmed by failure to obtain approval of the Fund for a contemplated action, and hence would be less reluctant to try giving up the privilege.

Restrictions on membership.

No restrictions as to membership should be imposed on grounds of the particular economic structure adopted by any country.

There are certain to be some persons or governments, who either out of fear, or prejudice, or dislike would wish to exclude countries with socialist economies from participation in an international undertaking of the character described in the previous pages. Yet to exclude a country such as Russia would be an egregious error. Russia, despite her socialist economy could both contribute and profit by participation. To deny her the privileges of joining in this cooperative effort to improve world economic relations would be to repeat the tragic errors of the last generation, and introduce a very discordant note in the new era millions everywhere are hoping for. If the Russian Government is willing to participate, her counsel in the preliminary negotiations should be as eagerly sought as that of any other country, and her membership in both Fund and Bank equally as welcome.

A socialist economy like a capitalistic economy engages in international trade and financial transactions which can be either beneficial or harmful to other countries. In fact, because the conduct of foreign trade and international financial transactions is so completely under the control of the government in a socialist economy, there is all the more reason to attempt to get them to join in a cooperative attempt to introduce stability in international economic relationships and a higher level of trade.

Furthermore, no one can know what direction some of the smaller liberated states will take in the shaping of their economic structures. There is likely to be, during the next decade or two, a variety of economic systems and it would seem desirable that these should not be discouraged from cooperating with the others so long as they are willing to agree to conduct their international economic affairs in accordance with principles acceptable to the United Nations.

IV. Composition of the Fund

The Fund shall consist of gold, member country currencies, and member government securities, in such amounts as shall be indicated by a formula set forth in the Agreements. The total subscription to the Fund shall be the equivalent of at least $5 billion.

The task which the Fund would be expected to perform would involve transactions of large magnitude; it therefore should have large resources available. Moreover, the greater its resources the more potent could the Fund be in preventing monetary disruption and in reducing the frequency and duration of periods of disequilibrium. Considering the likelihood that the number of participating governments might be at least a score, a total subscription of the equivalent of two to five billion dollars would seem to be both possible and desirable.

To avoid tying up funds that would not be needed for some time, if ever, the participants could be required to subscribe only 25 percent of their participation in cash. An additional 25 percent could be subscribed in obligations of the participating government. These obligations would yield revenue to the Fund, and would also supply a source of additional funds to be tapped if and when needed. They would also provide the Fund with the means of conducting open-market operations in any given country when desired. To reduce the cost to participating countries, it might be found preferable to make the securities a renewable three to five-year note, rather than a long-term bond, thus reducing the interest rate and increasing their marketability.

The remaining 50 percent of the subscription should be paid in such installments and in such form as shall be determined from time to time by the Fund.

The Fund would need local currencies and gold to carry on its operations. The provision that half the initial payment of 25 percent be in gold and half in local currencies takes care of that, and also makes participation easier for those countries having little gold. For a few of the countries—e.g. the United States—gold and local currencies are synonymous for purposes of international transactions. One of the objectives of the Fund is to increase the number of countries about which that could be said.

In view of the fact that the gains from participation in the Fund would not take the form of a distribution of substantial profits, the sum each member country should subscribe can hardly be left to the decision of each country. It is hoped that the Fund would show an annual profit but the purpose of the Fund is not to make profits but to help achieve much more important objectives that are not susceptible of measurement in terms of money profits. The Fund would be a cooperative enterprise operated for the benefit of all the participating nations, and each participant should subscribe at least its reasonable share of the total capital necessary, though it could subscribe more if it wished to do so. The share of the total each country subscribes should be determined by some agreed upon formula which would give due weight to various pertinent considerations.

There follows an illustrative formula that attempts to measure the minimum amount of funds each participant should be required to subscribe. The items listed are those which seem most pertinent, and the weights ascribed to each attempt roughly to reflect the importance of that item to the benefits that might be expected to result from participation and the ability to contribute to the Fund's capital.

1. Gold holdings	100	points for every billion dollars
2. Gold production	50	" " " " "
3. National income	2	" " " " "
4. Foreign trade	25	" " " " "
5. Population	1	" " " ten million
6. Foreign investments	25	" " " billion dollars
7. Foreign debts	10	" " " $50 million of annual interest payments on external public debt

Applying the above weights to the situation in some selected countries, the following approximate scores would result:

United States	2,905	U.S.S.R.	149
United Kingdom	577	China	78
Canada	125	Mexico	24
Netherlands and Colonies	143	Brazil	45
Norway	15	Colombia	12

Converted into dollars, the contributions would be something like the following:

TABLE
(In millions of U.S. dollars)

(Though the contributions or investments would be in the form of gold or local currency, they are converted, for convenience, into U.S. dollar units in the table below.)

United States	3,196	Argentina	72
England	635	Mexico	26
U.S.S.R.	164	Brazil	50
Canada	138	Colombia	13
Netherlands and Colonies	157	Cuba	9

The purpose of the table is merely to suggest a pattern of quotas for discussion, and not to lay down any precise pattern or formula. An attempt was made to present a pattern of quotas, the general character of which probably could be defended on logical grounds, but it is certain that a more appropriate formula could be worked out if several minds focused on the problem.

If only 50 percent of the participation were called for, and only half of that in cash, the amounts indicated in the above table would not be erroneous. The United States would be called upon to subscribe $500 million in cash and Cuba only $12½ million.

That would be the minimum. They could, of course, subscribe more if they wished. Experience would show whether the total was much more than was needed, or much less. If more were needed the securities could be converted into cash and the remaining half called in. On the other hand, if after long experience it is found that even the initial payments were greatly in excess of needs, it would be an easy matter to return the excess. Since the Fund should be ample to take care of periods of special stress, many years would have to pass, however, before enough experience is acquired to determine the most appropriate size of the Fund. It would certainly be better in the beginning to err on the side of having too much rather than not enough. The effective strength of the Fund and its ability to instill confidence in the currency stability of its participants will be enhanced with the ease with which the Fund can be expected to meet all legitimate claims on its resources. A sum of several billions of dollars does not, therefore, seem inappropriate to the task.

Inasmuch as some of the assistance the Fund can give to member countries is directly proportional to the sum of participation of that country, there will be a strong incentive for some countries to make their participation larger than the scheduled amount.

The Bank for Reconstruction and Development of the United and Associated Nations could be called upon to participate to the extent of possibly $100 million.

Contributions made according to the scale at the bottom of page 74 would result in total assets of $5,225,000,000. The following table summarizes the proportionate share which would be contributed by significant groups of countries. The second column of the table indicates the percentage of the total votes which would be allotted to each area, on the basis of these minimum contributions.

	Participation	Number of Votes on Board
	(In percent of total)	
United States	61.03	25.32
Argentina and Chile	1.68	3.93
Other Latin America	2.93	30.54
British Empire	20.20	17.56
U.S.S.R.	3.13	2.85
Netherlands and Colonies	3.01	2.81
Other European Countries	4.24	13.10
China	1.64	2.26
Bank for Reconstruction	2.14	1.63
	100.00	100.00

V. Management

Where control of the Fund shall be vested is a matter of paramount importance in the formulation of a workable plan. The magnitude of the Fund, the broad scope of its likely powers, the requirements for continued eligibility of participants, together make the question of situs of control important.

The management of the Fund should be vested in a Board of Directors consisting of the representatives appointed by the member governments, each government to appoint one representative.

It would be easy to reach agreement that the most convenient and simplest device would be to vest control of the Fund in a board of directors, to consist of representatives appointed by member governments, each government appointing one representative. It probably would be desirable to have each government appoint an alternate as well. In view of the technical nature of many of the problems, the governments might wish to select as alternates men who would be more qualified than are likely to be the representatives to take up the kind of problems that would most frequently come before the Fund. The representatives would probably be selected from more responsible posts than the alternates, and would likely be concerned with the larger and less technical issues involved in decisions.

The Board shall elect a chairman and a small operating committee.

With a body so unwieldy as it would likely be with representatives from each government, added to the fact that many of such representatives could devote only brief periods away from their home governments, it is virtually essential that the day-to-day operations of the Fund be handled by a small operating committee of representatives. Such a committee would be able to devote full time to the task of managing the Fund, and would, of course, have to be adequately compensated. The election of this operating committee by the member participants would insure the selection of a competent group and the brief period of their tenure of office before reelection would assure also a responsiveness to the wishes of the board. Delegation of authority by the whole board to the committee on many matters could be safely made, leaving larger policy decisions to be referred to the entire board. It is to be expected that the operating committee would have the assistance of a competent technical staff.

If a Fund were to be established with anything like the powers and resources outlined in this report, it would need the services of a large staff of the best experts available. Nothing would injure the chances of effective and successful operation and of making a major contribution to the solution of some of our most troublesome international economic problems than mediocrity in directors and technical staff. A board the size of the one recommended here can, of course, assimilate without serious damage some stuffed shirts, some narrow-minded nationalists, and a few bankers with counting house ideals. But the board will have to include more than a sprinkling of economic statesmen, forward looking and of broad vision, comprehensive experienced world outlook and tenacity of social purpose. The technical staff will have to be headed up by experienced analysts with a thorough knowledge of monetary theory and international economics, with intellectual integrity and aggressiveness, and also include a generous quota of eager, able, young men who have been at or near the top in their scholastic achievements and technical writings. The United and Associated Nations can produce plenty of such men.

In all voting by the Board, each representative should have one hundred votes, plus one vote for the equivalent of every million dollars turned over to the Fund.

There would be little difficulty in reaching agreement that some such set-up as the board working through a committee as outlined above would provide a satisfactory working arrangement, but the real problem is how to distribute the voting power. If each member of the board were to be given an equal vote, then a small country that invested one million dollars would have as much power in making decisions as a country that has subscribed a hundred or a thousand times that amount. With the possibility that the number of small countries participating will be much greater than the large countries, a one-vote-one-member arrangement is palpably unwise. On the other hand, to accord voting power strictly proportionate to the value of the subscription would give the one or two powers control over the Fund. To do that would destroy the truly international character of the Fund, and seriously jeopardize its success. Indeed, it is very doubtful if many countries would be willing to participate in an international organization with wide powers if one or two countries were to be able to control its policies.

It is clear that the voting power must be so arranged as to steer between these two evils. This might be accomplished by working out some compromise between the two bases of voting power referred to above. By giving each member 100 votes plus one vote for every million dollars invested in the Fund, a satisfactory distribution of control might be approximated. Thus, if the United States subscribes $1 billion it would have 100 plus 1,000 votes, or a total of 1,100 votes, whereas a country contributing $10 million would have 100 plus 10 votes, or a total of 110. With such an arrangement ten small countries could outvote the United States. If any country felt the arrangement agreed upon did not give it an adequate share of control, it could increase its contribution.

A country should have the privilege of replacing, wholly or in part, its securities, with currency or gold. The number of votes its representatives can cast would alter accordingly.

This provision would supply some flexibility in the assets a country turns over to the Fund, and also provides a means whereby a country could increase its voting power. How important the provision might prove to be is uncertain, but in the beginning at least it would appear desirable to introduce flexibility wherever possible.

All decisions, except where specifically provided otherwise, should be decided by a simple majority of the votes cast.

To give adequate protection to each country, most of the important decisions could be made to require more than a simple majority of the votes.

The President of the Bank should be a member of the Board, and would have 100 votes.

Because of the interdependence of the two institutions—the Fund and the Bank—close liaison and opportunities to harmonize policies would be helpful. Both agencies would have broad objectives, both would be international in their outlook, and both would be motivated by the desire to promote worldwide peace, prosperity, and stability. Each would be undertaking responsibilities that call for analyses and judgments of economic situations and trends. The operations of each would affect the other, and the decisions of each should be partly based on the knowledge, plan and judgment of the other. There, therefore, is much to be gained by close liaison between them. That is why the head of each should be a director of the other.

To avoid cumulating voting power, however, the Bank should not be able to cast votes in excess of the minimum, irrespective of the extent of its monetary participation.

Reports and information

The possession by the Fund of adequate, timely and appropriate information is a vital necessity to its proper functioning. The Fund should have the authority to require that all members file with it a quarterly itemized balance of payments. This balance of payments record—which is of particular importance in the operation of this Fund—should be standardized in form, and carefully designed by the technical staff of the Fund. The Fund would also need special reports from members from time to time, and should have the authority to obtain them.

[The following paragraphs are from Part III, commenting on the plans for an International Bank.]

A new international currency

We frequently hear expressed a desire or hope for a new international currency, but the specific nature of the new currency is never described, nor are the gains that are presumed to result from such a currency ever stated in meaningful language. They are either taken for granted or referred to only in the vaguest of generalities. So much misunderstanding of the nature and utility of a new international currency seems to prevail that it is probably worth attempting to indicate the limits of usefulness possessed by such a currency. The reader not interested in the confusions surrounding the demand for an international currency can omit the next few pages.

There are some persons who seem to think that all foreign exchange problems would be solved if only all countries adopted the same international unit for use in international transactions. A little thought will demonstrate how absurd that belief is. The fact that Canada adopted a "dollar" unit containing 100 cents and having the same *de jure* gold content as the United States dollar, did not prevent the adoption of foreign exchange controls in Canada nor did it keep the United States dollar-Canadian dollar exchange rate from moving, any more than did Australia, South Africa and New Zealand, by adopting the same unit as England, prevent the value of the currencies of those countries from changing in relation to the British £ sterling. There are innumerable instances of different currency units keeping the same value, in terms of each other, for many years; and other instances of similar currency units beginning with identical values and only to have those values change greatly. Thus, the pound sterling hovered around $4.86 for thirty-five years (1878–1914), and the Swiss franc was about 20 cents for fifty years; whereas, the exchange rates between the British £ and Australian £ and New Zealand £ and the Egyptian £ have moved greatly notwithstanding the fact that to begin with they all were the same unit, not only in designation—pound—but in the sense that their value was 1 to 1.

The value of any currency in terms of any other currency is a consequence of a complex of monetary and economic forces, changes in these forces influence the value of one currency in terms of others. The adoption of a new international currency would not modify those forces one whit. If all of the Western Hemisphere were to adopt the "dollar" as their own unit of currency, it would not be long before it would be necessary to distinguish between the "U. S. dollar," the "Mexican dollar," the "Colombian dollar," etc., because the exchange rates between those currencies had moved away from the 1 to 1 ratio. In fact, even now there are a number of "dollars" in use in the foreign exchange systems of the American Republics. The adoption of the same unit of currency no more eliminates foreign exchange problems than would the general adoption of Esperanto solve international political problems or no more than does the use of a common language, e.g. Spanish, eliminate international political problems between all Spanish-speaking nations.

Occasionally, one hears expressed the view that if only there could be created some unit of currency that could be universally used in trade—"a trade dollar" or "export dollar" (Presumably no reference is intended to a special kind of dollar which costs less to the foreigner than a regular dollar, yet which buys as much in the U. S. as a regular dollar. That would be a clear example of multiple currencies which involve government subsidies, and which constitutes one of the devices the U. S. is opposed to on principle), or any unit with a new name—considerable advantages in trade and other international transactions would result. Unfortunately, this view is fallacious. The obstacles to trade do not lie in the fact that different countries use different units of currency. Insofar as currency has anything to do with obstructing trade, it is the scarcity of foreign exchange and the variations in exchange rates which are responsible. Neither of these two obstacles to trade will be dissipated by the adoption of a new international unit of currency. There are, it is true, possibilities of developing machinery which will make foreign exchange more plentiful to countries that lack adequate foreign exchange, and there is also machinery which may be developed to reduce the fluctuation in exchange rates. The proposal here made for the Fund and the Bank is designed to help achieve those very objectives among others. Neither proposal involves, or needs, or is dependent upon the adoption of an international unit of currency.

We already have an international medium of exchange, namely, gold. An ounce of gold .999 fine is the same in United States as it is in China or South Africa or Iceland. Any exporter or importer or banker or investor can liquidate a monetary debt with gold just as easily as would be possible with a new international unit. Such difficulties as exist in the use of gold as a medium of international exchange lie in difficulties imposed by war conditions. In peace time nothing could be simpler than to send or receive gold, or send or receive dollar or other exchange convertible into gold.

Some who clamor for a new international currency to replace gold would concede this, but claim gold is too expensive to be used. This is quite another matter. It may be possible to develop a satisfactory international medium of exchange that costs less to produce than more gold, but certainly not significantly less than gold already in monetary stock. It is important to remember in thinking about this subject that the monetary gold stock of the country *has already been paid for. It is very inexpensive to use the gold already in world monetary stocks.* Even the cost of shipping from one country to another can be avoided through development of earmarking. The only expense of using gold already mined is the small value that gold would have for industrial uses if it had no monetary value.

The situation is quite different with respect to further additions to the gold stock—and more complex. Obviously there is a real cost as well as a monetary cost involved in mining and refining gold. Insofar as the gold would not be produced had it only commodity value, and insofar as the labor and material used in gold mining would be used for some other purpose, it is true that additions to our monetary gold stock are expensive. The solution to that, however, is simple—namely, just limit or control the additions of newly-mined gold to the world's monetary stock. This is not the place to discuss the method; suffice to say it is entirely feasible should it ever be deemed desirable. There are some advantages and disadvantages to the proposal, but it is possible that the time may come when the advantages may outweigh the disadvantages. In any case, the utility of *additions* to the world's monetary stock is a separate question from that of use of *existing* stocks. There is no advantage in substituting a new medium of international exchange for existing gold—even if it could be done—and I am confident it could not be done. But it may be worthwhile giving the Bank note-issuing powers—based on some gold reserve—solely in order to make the world's monetary gold stock do more work, and at the same time help correct the maldistribution of gold.

To be sure, the United States already does just that when for one reason or another, by one method or another, it increases its supply of currency and demand deposits.

The only difference between what the United States (and virtually every other country) already does, and what it is proposed the Bank shall do is that in the United States note issues are regulated by the law of the country, whereas the proposed note issues of the Bank will be regulated by the by-laws of the Bank as drawn up by the member Governments.

The belief previously referred to as being held in some quarters that a common unit of currency will solve the world's foreign exchange problems, and help promote foreign trade in goods and services, and the international flow of capital does not concern itself with either the scarcity of gold, or its maldistribution. It seems to take the form of something much less intelligible. It seems to assume that these benefits are to be attained by a new international unit which is to be adopted by many countries as a *substitute* for their own currency.

The belief that countries will find it helpful to replace their own currency in favor of a currency to be used by all, or by a group of nations, is based on a fundamental misunderstanding of the factors which determine the value of any currency. So long as most countries insist on shaping their own monetary policies so long will it be impossible to replace local currencies with a new international currency. The adoption of a common currency by several countries is possible only if they each surrender separate sovereignty in monetary and credit policies in favor of sovereignty exercised by one over all of them, or by an international organization. For example, it was impossible for the states in the American colonies to have a common currency with a common value until the United States was formed and the Federal Government given sole authority over currency. Even then scores of different bank notes existed, many of them with changing values, because the State rather than the Federal Government exercised sovereignty in matters of bank note issue. It was only until the Federal Government became supreme in the matter of all note issues that the United States was able to keep all bank notes at par.

It is possible for a group of countries to agree to adopt a common currency, but such adoption is of little use unless they also agree not to exercise separate sovereign powers with respect to note issues, exchange rates, rediscount rates and privileges and other aspects of monetary policy. If country A is going to agree to adopt the same currency as country B, country A will want assurance that country B cannot do whatever it pleases with its monetary policy.

But, it may be asked, would not the use of a new international unit as a *supplement* to local currency facilitate international trade and finance? The answer is an unqualified "No."

A "trade dollar" or "Demos" or "Victor" or "what-have-you" unit of currency supplementing the United States dollar, whether of the same or different value, would no more help foreign trade than would the adoption of a new flag. The only difference in trade between Massachusetts and Texas and trade between Massachusetts and Mexico—aside from tariffs—is that in the first case both buyer and seller deal in dollars only, whereas in trade between Mexico and United States two currencies are involved—the Mexican peso and United States dollar. (The supply of either currency to either country would be no different with a supplementary currency than without it; therefore, the matter of supply and demand for currency can be ignored in this discussion.) An importer, exporter, bank, or a tourist has simply to make conversions from one currency into another in his transactions. Were it possible to eliminate by use of an international currency unit the arithmetical labors involved in the conversions, it would indeed be a convenient device, though by no means a very important one. Unfortunately, however, the use of a new international currency unit does not obviate the necessity of calculating conversion values any more than does the use of gold in settling international transactions.

Let us, for example, consider the case of a tourist. As it is now, when an American travels to Mexico he converts his dollars into Mexican pesos, when he enters Colombia he converts his dollars into Colombian pesos, and when he goes to Brazil he converts his dollars into milreis, etc. Yet, if there existed a new international unit of currency he would be no better off; his purchases and sales would be consummated with no less inconvenience. On the contrary, he would have to make more calculations and more monetary adjustments in his price judgments. Upon leaving the United States he would have to convert his dollars into the new international unit and then when he came to Mexico he'd have to convert the international unit into pesos since most prices in any country are expressed in terms of the local currency unit. He would have had to do just that had he carried with him dollars instead of an international currency. Only this time, if he wanted to judge the value of an article tagged, say 50 pesos, he would have to make two mental conversions instead of one, because most of his life he has been dealing in dollars and cents, not in a new international currency. Then, when he enters Colombia he would have to again calculate conversions and again make the necessary mental adjustments in evaluating his purchases. It would be possible, of course, to have price tags or price schedules in shops and hotels frequented by tourists expressed in the international unit, but such a practice would be a nuisance to the seller and would be only a slight convenience to the buyer.

Nor does a buyer of imported goods purchase those goods in one country rather than in another because of ease of an arithmetical calculation. Where there is any difficulty and the seller meets with any sales resistance on this score, he can easily overcome it by quoting his price in the buyer's currency even if a bill is to be paid in the seller's currency.

Is there then no advantage to be obtained from the adoption of a new international unit of currency aside from the advantage of increasing the Bank's lending resources described earlier?

Yes, there is one advantage, though of minor importance. It is in the realm of economic research. A universally recognized international monetary unit of account would be helpful in the presentation of those statistical series which are pertinent to international comparisons and of use in discussions involving international comparisons of quantitative data measured in money terms. For many purposes it would be convenient to set up tables that involved summation of money values in more than one currency. It would also prove useful in statistical data involving comparisons of various money values over long periods of time.

Were values set in terms of a local currency which had undergone substantial changes in purchasing power relative to other countries, certain significant comparisons would be easier to make.

Altogether, the introduction of a new currency unit would not be of sufficient importance to warrant its introduction at this time, were the Bank not to be established with note issuing power. But if the Bank were to be established and given the authority to issue notes, what unit should it be?

It would probably be preferable to adopt a new unit. The adoption of a new international unit of currency of account would probably meet with little opposition, whereas an attempt to use any one of the existing currencies, such as dollars, sterling, or francs for that purpose would be opposed on the grounds that it would seem to give the country possessing that currency some slight advantage in publicity or trade. There are deemed to be some national prestige values and possibly slight economic gains in trade and financial transactions that adhere to a country having a currency that is widely used as an international unit of account. For that reason a new unit belonging to no country would be more welcome to most countries than the unit of any selected country.

A new unit of currency would have to be defined. It would have to be fixed in terms of something, whether by international agreement or by general acquiescence, or unilateral action. To set the value of the new currency unit in terms of some existing currency has the disadvantage of subjecting the new unit to the variations of the currency to which it is tied and also raises the question of "favoritism." The simplest course is to fix the value of the new unit in terms of gold. A unit of account does not have to be set in terms of gold, it could be set in terms of some commodity other than gold—tin, platinum, or any material. It could even be set in terms of an average basket of goods, or an aggregate of goods. But examination of the various possibilities will show that the only practical solution is to set the new currency unit in terms of a given physical volume of gold.

For convenience of arithmetical calculation it would probably be well to define the new unit as being equivalent to 14.62 grains nine-tenths fine. This would make the new unit worth 50 U.S. [cents] or 10 yuan or 2 s. at current rates of exchange and at present price for gold in the United States.

(B) Preliminary Draft Outline of a Proposal for an International Stabilization Fund of the United and Associated Nations

(Revised July 10, 1943)

The plan for post-war international currency stability set forth in this pamphlet is a revision of the preliminary draft outline of a proposal for an International Stabilization Fund of the United and Associated Nations made public by the Secretary of the Treasury on April 7, 1943.

The preliminary draft was sent by the Secretary of the Treasury to the finance ministers of the United Nations and the countries associated with them with a request that it be studied by their technical experts. The finance ministers were also invited to send representatives to Washington for informal discussions with the experts of this Government.

Such informal discussions have been held with nearly 30 countries. On the basis of these discussions, the experts of the Treasury with the cooperation of experts of other Departments of this Government have revised the preliminary draft proposal for an international stabilization fund. While suggestions of the representatives of other countries have been included in the revised draft, it does not necessarily reflect the views of the experts of any other country.

This revised draft is in every sense still a preliminary document representing the views of the technical experts of the Treasury and of other Departments of this Government. It has not received the official approval either of the Treasury or this Government.

FOREWORD

By HENRY MORGENTHAU, Jr., *Secretary of the Treasury*

When the United Nations have brought this war to a successful conclusion, they will be faced with many urgent international economic and financial problems. Some of these are new problems arising directly from this war; others are continuing consequences of failure to solve the problems that have been with us since the last war. The solution of these problems is essential to the development of a sound economic foundation for world peace and prosperity.

All of the important international economic and financial problems are closely interrelated. Monetary stabilization, commercial policy, the provision of long-term international credit, promotion of stability in the prices of primary products, and arrangements for relief and rehabilitation are problems that join at innumerable points. Nevertheless, because of their complexity, they must be taken up separately, although each in turn must be integrated with the rest.

It is generally recognized that monetary stability and protection against discriminatory currency practices are essential bases for the revival of international commerce and finance. For this reason, an appropriate starting point might well be the consideration of post-war international monetary problems. Success in dealing with international monetary problems in the post-war period will contribute toward final solution of the other international financial and economic problems. Despite the technical difficulties involved, the common interest which all countries have in the solution of post-war monetary problems provides a basis for agreement.

It is still too soon to know the precise form and magnitude of post-war monetary problems. But it is certain that we shall be confronted with three inseparable monetary tasks: to prevent the disruption of foreign exchanges, to avoid the collapse of monetary systems, and to facilitate the restoration and balanced growth of international trade. Clearly, such formidable problems can be successfully handled only through international action.

The creation of instrumentalities adequate to deal with the inevitable post-war monetary problems should not be postponed until the end of hostilities. It would be ill-advised, if not dangerous, to leave ourselves unprepared at the end of the war for the difficult taks of international monetary cooperation. Specific and practical proposals must be formulated by the experts and must be carefully considered by the policy-shaping officials of the various countries. In each country acceptance of a definitive plan can follow only upon legislative or executive action. And even when a plan is finally adopted, much time will be consumed in preparation before an international institution for monetary cooperation can begin effective work.

There is another important reason for initiating now concrete discussions of specific proposals. A plan for international monetary cooperation can be a factor in winning the war. It has been suggested, and with much cogency, that the task of assuring the defeat of the Axis powers would be made easier if the victims of aggression could have greater assurance that a victory of the United Nations will not mean in the economic sphere a repetition of the exchange instability and monetary collapse that followed the last war. The people in all of the United Nations must be given some assurance that there will not again be two decades of post-war economic disruption. The people must know that we at last recognize the fundamental truth that the prosperity of each country is closely linked to the prosperity of other countries.

One of the appropriate agencies to deal with international economic and monetary problems would be an international stabilization fund with resources and powers adequate to the task of helping to achieve monetary stability and of facilitating the restoration and balanced growth of international trade. A proposal along these lines was drafted by American technical experts and made public on April 7, 1943. There have been informal discussions on this draft in which nearly thirty countries have participated. These discussions have shown that all countries think joint action in this field is necessary for the reconstruction of the world economy.

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 may be needed to provide long-term international credit for post-war reconstruction and development, to provide funds for rehabilitation and relief, and to promote stability in the prices of primary international commodities. There is a strong inclination on the part of some to entrust to a single agency the responsibility for dealing with these and other international economic problems. We believe, however, that an international economic institution can operate most effectively if it is not burdened with diverse duties of a specialized character.

Although an international stabilization fund can provide the facilities for cooperation on monetary questions, the establishment of such an institution would not of itself assure the solution of these difficult problems. The operations of such a fund can be successful only if the powers and resources of the fund are used wisely, and if member countries cooperate with the fund's endeavors to maintain international equilibrium at a high level of international trade. Such cooperation must include commercial policies designed to reduce trade barriers and to terminate discriminatory practices that have in the past hampered the balanced growth of international trade. The nations of this world can be prosperous only if they are good neighbors in their economic as well as their political relations.

The draft proposals that have been put forward on a tentative basis have received wide publicity in the United States, the United Kingdom, Canada, and in other countries. It is in the best democratic tradition that the people should have the fullest opportunity to express their views and to shape the policies of their Governments on the important problems affecting national well-being. And it is an extension of this tradition that all the United Nations should have an opportunity to participate in the formulation of a program for international monetary cooperation.

This revised draft is published with the hope that it will call forth further comments and constructive suggestions. It aims to present only the essential elements of a workable international stabilization fund, and its provisions are in every sense tentative. Obviously, there are many details that have been omitted and that can be better formulated after there is agreement on the more important points. We believe that a workable and acceptable plan can emerge only from the joint efforts of the United Nations support by enlightened public opinion.

PRELIMINARY DRAFT OUTLINE OF A PROPOSAL FOR AN INTERNATIONAL STABILIZATION FUND OF THE UNITED AND ASSOCIATED NATIONS

Preamble

1. There is a growing recognition that progress toward establishment of a functioning democratic world in the post-war period will depend on the ability of free peoples to work together in solving their economic problems. Not the least of these is the problem of how to prevent a widespread breakdown of currencies with resultant international economic disorder. We must assure a troubled world that the free countries will solve these perplexing problems, and that they will not resort to competitive exchange depreciation, multiple currency practices, discriminatory bilateral clearing, or other destructive foreign exchange devices.

2. These are not transitory problems of the immediate postwar period affecting only a few countries. The history of the past two decades shows that they are continuing problems of vital interest to all countries. There must be a general realization that world prosperity, like world peace, is indivisible. Nations must act together to restore multilateral international trade, and to provide orderly procedure for the maintenance of balanced economic growth. Only through international cooperation will it be possible for countries successfully to apply measures directed toward attaining and maintaining a high level of employment and income which must be the primary objective of economic policy.

3. The International Stabilization Fund of the United and Associated Nations is proposed as a permanent institution for international monetary cooperation. The

resources of this Fund would be available under adequate safeguards to maintain currency stability, while giving member countries time to correct maladjustments in their balance of payments without resorting to extreme measures destructive of international prosperity. The resources of the Fund would not be used to prolong a basically unbalanced international position. On the contrary, the Fund would be influential in inducing countries to pursue policies making for an orderly return to equilibrium.

4. The Fund would deal only with member governments and their fiscal agents, and would not intrude in the customary channels for conducting international commerce and finance. The Fund is intended to provide supplemental facilities for the successful functioning of the established foreign exchange institutions and to free international commerce from harmful restrictions.

5. The success of the Fund must ultimately depend upon the willingness of nations to act together on their common problems. International monetary cooperation should not be regarded as a matter of generosity. All countries have a vital interest in the maintenance of international monetary stability, and in the balanced growth of multilateral international trade.

I. Purposes of the Fund

The United Nations and the countries associated with them recognize, as declared in the Atlantic Charter, the need for the fullest cooperation among nations with the object of securing economic advancement and rising standards of living for all. They believe that attainment of these objectives will be facilitated by international monetary cooperation. Therefore, it is proposed that there be established an International Stabilization Fund with the following purposes:

1. To help stabilize the foreign exchange rates of the currencies of the United Nations and the countries associated with them.

2. To shorten the periods and lessen the degree of disequilibrium in the international balance of payments of member countries.

3. To help create conditions under which the smooth flow of foreign trade and of productive capital among the member countries will be fostered.

4. To facilitate the effective utilization of the blocked foreign balances accumulating in some countries as a consequence of the war situation.

5. To reduce the use of such foreign exchange restrictions, bilateral clearing arrangements, multiple currency devices, and discriminatory foreign exchange practices as hamper world trade and the international flow of productive capital.

II. Composition of the Fund

1. The Fund shall consist of gold and the currencies and securities of member governments.

2. Each of the member countries shall subscribe a specified amount, to be called its *quota*. The aggregate of quotas of the member countries shall be the equivalent of at least $5 billion.

3. Each member country shall meet its quota contribution in full on or before the date set by the Board of Directors for the Fund's operations to begin.

(a) A country shall pay in gold not less than an amount determined as follows. If its gold and free foreign exchange holdings are:

(i) In excess of three times its quota, it shall pay in gold 50 percent of its quota.

(ii) More than two but less than three times its quota, it shall pay in gold 40 percent of its quota plus 10 percent of its holdings in excess of twice its quota.

(iii) More than its quota but less than twice its quota, it shall pay in gold 30 percent of its quota plus 10 percent of its holdings in excess of its quota.

(iv) Less than its quota, it shall pay in gold 30 percent of its holdings.

The gold payment required of a member country substantial parts of whose home areas have been wholly or partly occupied by the enemy, shall be only three-fourths of the above. (For other gold provisions, Cf. V–2–a and V–6, 7.)

A member country may include in the legal reserve account and in the published statement of the reserves of gold and foreign exchange in its Treasury or Central Bank, an amount not to exceed its gold contribution to the Fund, minus its net purchases of foreign exchange from the Fund paid for with local currency.

(*b*) It shall pay the remainder of its quota in local currency, except that a member country may substitute government securities (redeemable at par) for local currency up to 50 percent of its quota.

4. A quota for each member country shall be computed by an agreed upon formula which gives due weight to the important relevant factors, *e. g.*, a country's holdings of gold and free foreign exchange, the magnitude and the fluctuations of its balance of international payments, its national income, *etc.*

Before computing individual quotas on the basis of the agreed upon formula, there shall be reserved an amount equal to 10 percent of aggregate quotas to be used as a special allotment for the equitable adjustment of quotas. Where the initial quota of a member country as computed by the formula is clearly inequitable, the quota may be increased from this special allotment.

5. Quotas shall be adjusted on the basis of the most recent data 3 years after the establishment of the Fund, and at intervals of 5 years thereafter, in accordance with the agreed upon formula. In the period between adjustment of quotas, the Fund may increase the quota of a country, where it is clearly inequitable, out of the special allotment reserved for the equitable adjustment of quotas.

6. Any changes in the formula by which the quotas of member countries are determined shall be made only with the approval of a four-fifths vote of the Board.

7. No increase shall be made in the quota of a member country under II–4, 5 or 6 without the consent of the representative of the country concerned.

8. The resources of the Fund shall be used exclusively for the benefit of the member countries.

III. Monetary Unit of the Fund

1. The monetary unit of the Fund shall be the *unitas* (~~UN~~) equal in value to $137\frac{1}{7}$ grains of fine gold (equivalent to $10). No change in the gold value of the unitas shall be made except with the approval of 85 percent of the member votes. When such change is made, the gain or loss sustained by the Fund on its holdings of gold shall be distributed equitably among the members of the Fund.

The accounts of the Fund shall be kept and published in terms of unitas.

2. The value of the currency of each member country shall be established in terms of unitas and may not be altered except as provided in IV–5, below. (Cf. IV–1, 2, below.)

No member country shall purchase or acquire gold, directly or indirectly, at a price in terms of its national currency in excess of the parity which corresponds to the value of its currency in terms of unitas and to the value of unitas in terms of gold; nor shall any member country sell or dispose of gold, directly or indirectly, at a price in terms of its national currency below the parity which corresponds to the value of its currency in terms of unitas and to the value of unitas in terms of gold. (Cf. VII–1.)

3. No change in the value of the currencies of member countries shall be permitted to alter the value in unitas of the assets of the Fund. Whenever the currency of a member country has depreciated to a significant extent, that country must deliver to the Fund when requested an amount of its local currency or securities equal to the decrease in the unitas value of the Fund's holdings of the local currency and securities of the country. Likewise, if the currency of a member country should appreciate to a significant extent, the Fund must return to that country an amount (in the currency or securities of that country) equal to the resulting increase in the unitas value of the Fund's holdings.

IV. Exchange Rates

1. The rates at which the Fund will buy and sell one member currency for another and at which the Fund will buy and sell gold for local currency shall be established in accordance with the provisions below. (Cf. also III–2 and V–2.)

2. The initial rates of exchange for member countries' currencies shall be determined as follows:

(a) For any country which becomes a member prior to the date on which the Fund's operations begin, the rates initially used by the Fund shall be based upon the value of the currency in terms of United States dollars which prevailed on July 1, 1943.

If, in the judgment of either the member country or the Fund, the above rate is clearly inappropriate, the initial rate shall be determined by consultation between the member country and the Fund. No operations in such currency shall be undertaken by the Fund until a rate has been established which has the approval of the Fund and of the member country in question.

(b) For any member country which has been occupied by the enemy, the Fund shall use the exchange rate fixed by the government of the liberated country in consultation with the Fund and acceptable to the Fund. Prior to the fixing of a definitive rate, operations in such currency may be undertaken by the Fund with the approval of the Board at a tentative rate of exchange fixed by the member country in consultation with the Board. No operations shall be continued under this provision for more than 3 months after the liberation of the country or when the local currency holdings of the Fund exceed the quota of the country, except that under special circumstances the period and the amount of such operations may be extended by the Fund.

3. The Fund shall not come into operation until agreement has been reached on the exchange rates for currencies of countries representing a majority of the aggregate quotas.

4. The Fund shall determine the range within which the rates of exchange of member currencies shall be permitted to fluctuate. (Cf. VII–1.)

5. Changes in the exchange value of the currency of a member country shall be considered only when essential to the correction of fundamental disequilibrium in its balance of payments, and shall be made only with the approval of three-fourths of the member votes including the representative of the country concerned.

Because of the extreme uncertainties of the immediate post-war period, the following exceptional provisions may be used during the first 3 years of the Fund's operations:

(a) When the existing rate of exchange of a member country is clearly inconsistent with the maintenance of a balanced international payments position for that country, changes from the established rate may be made at the special request of that country and with the approval of a majority of the member votes.

(b) A member country may change the established rate for its currency by not more than 10 percent provided that the member country shall notify the Fund of its intention and shall consult with the Fund on the advisability of its action.

V. Powers and Operations

The Fund shall have the following powers:

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

The Fund shall purchase for local currency or needed foreign exchange any member currency in good standing acquired by another member country in settlement of a balance of payments on current account, where such currency cannot be disposed of in the foreign exchange markets within the range established by the Fund.

2. To sell to the Treasury of any member country (or Stabilization Fund or Central Bank acting as its agent) at the accepted rate of exchange, currency of any member country which the Fund holds, provided that:

(a) The foreign exchange demanded from the Fund is required to meet an adverse balance of payments predominantly on current account with any member country. (Cf. V–3, for capital transfers.)

When the gold and free foreign exchange holdings of a member country exceed 50 percent of its quota, the Fund in selling foreign exchange to such member country shall require that one-half of such exchange shall be paid for with gold or foreign exchange acceptable to the Fund. (Cf. V–6, 7; on gold collateral, see V–2–c.)

(b) The Fund's total holdings of the currency and securities of any member country shall not exceed the quota of such country by more than 50 percent during the first year of operation of the Fund, and thereafter shall not exceed such quota by more than 100 percent (except as otherwise provided below). The total holdings thus permitted are termed the *permissible quota* of a country. When the Fund's holdings of local currency and securities are equal to the permissible quota of a country, the Fund may sell foreign exchange for such additional local currency only with the specific approval of the Board of Directors (cf. VI–3–a, below), and provided that at least one of the following two conditions is met:

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

(ii) It is believed that the balance of payments of the country whose currency is acquired by the Fund will be such as to warrant the expectation that the excess currency holdings of the Fund can be disposed of within a reasonable time;

Provided further, that when the Fund's holdings of the currency of any member country or countries fall below 20 percent of their respective quotas, the sale shall also require the approval of the representatives of these countries.

(*c*) When the Fund's holdings of local currency and securities exceed the permissible quota of a country, the Board may require the member country to deposit collateral in accordance with regulations prescribed by the Board. Such collateral shall take the form of gold, foreign or domestic currency or Government bonds, or other suitable collateral within the capacity of the member country.

(*d*) When, in the judgment of the Fund, a member country, whose currency and securities held by the Fund exceed its quota, is exhausting its permissible quota more rapidly than is 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.

3. The Fund may sell foreign exchange to a member country, under conditions prescribed by the Fund, to facilitate a transfer of capital, or repayment or adjustment of foreign debts, when in the judgment of the Board such a transfer is desirable from the point of view of the general international economic situation, provided the Fund's holdings of the currency and securities of the member country do not exceed 150 percent of the quota of that country. When the Fund's holdings of the local currency and securities of a member country exceed 150 percent of the quota of that country, the Fund may, in exceptional circumstances, sell foreign exchange to the member country for the above purposes with the approval of three-fourths of the member votes. (Cf. V–2–a, above; on voting, VI–3–a, below.)

4. 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 shall render a report to that country. The report shall embody an analysis of the causes of the depletion of the Fund's holdings of that currency, a forecast of the prospective balance of payments in the absence of special measures, and finally, recommendations designed to increase the Fund's holdings of that currency. The representative of the country in question shall be a member of the Fund committee appointed to draft the report. This report shall be sent to all member countries and, if deemed desirable, be made public. Member countries agree that they will give immediate and careful attention to recommendations made by the Fund.

5. Whenever it becomes evident to the Board of Directors that the anticipated demand for any particular currency may soon exhaust the Fund's holdings of that currency, the Fund shall inform the member countries of the probable supply of the currency and of a proposed method for its equitable distribution, together with suggestions for helping to equate the anticipated demand for and supply of that currency.

The Fund shall make every effort to increase the supply of the scarce currency by acquiring that currency from the foreign balances of member countries. 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.

To facilitate appropriate adjustment in the balance of payments position of member countries, and to help correct the distortions in the pattern of trade balances, the Fund shall apportion its sales of such scarce currency. In such apportionment, it shall be guided by the principle of satisfying the most urgent needs from the point of view of the general international economic situation. It shall also consider the special needs and resources of the particular countries making the request for the scarce currency.

The right of any member country to acquire an amount of other currencies equal to its permissible quota shall be limited by the necessity of assuring an appropriate distribution among the various members of any currency the supply of which is scarce.

6. In order to promote the most effective use of the available and accumulating supply of foreign exchange resources of member countries, each member country agrees that it will offer to sell to the Fund, for its local currency or for foreign currencies which the member country needs, one-half of the foreign exchange resources and gold it acquires in excess of its official holdings at the time it became a member of the Fund, but no country need sell gold or foreign exchange under this provision unless its official holdings (*i. e.*, Treasury, Central Bank, Stabilization Fund, *etc.*) are in excess of 25 percent of its quota. For the purpose of this provision, only free and liquid foreign exchange resources and gold shall be considered. The Fund may accept or reject the offer. (Cf. II–3–a, V–2–a, and V–7.)

To help achieve this objective each member country agrees to discourage the excessive accumulation of foreign exchange resources and gold by its nationals. The Fund shall inform any member country when, in its opinion, any further growth of privately held foreign exchange resources and gold appears unwarranted.

7. When the Fund's holdings of the local currency and securities of a member country exceed the quota of that country, the Fund shall, upon request of the member country, resell to the member country the Fund's excess holdings of the currency of that country for gold or acceptable foreign exchange. (Cf. V–14, for charges on holdings in excess of quota.)

8. To buy from the governments of member countries, blocked foreign balances held in other member countries, provided all the following conditions are met:

(*a*) The blocked balances are held in member countries and are reported as such (for the purpose of this provision) by the member governments and are verified by the Fund.

(*b*) The member country selling the blocked balances to the Fund agrees to transfer these balances to the Fund and to repurchase from the Fund 40 percent of them (at the same price) with gold or such free currencies as the Fund may wish to accept, at the rate of 2 percent of the transferred balances each year for 20 years beginning not later than 3 years after the date of transfer.

(*c*) The country in which the blocked balances are held agrees to transfer to the Fund the balances described in (*b*) above, and to repurchase from the Fund 40 percent of them (at the same price) with gold or such free currencies as the Fund may wish to accept, at the rate of 2 percent of the transferred balances each year for 20 years beginning not later than 3 years after the date of transfer.

(*d*) A charge of 1 percent on the amount of blocked balances sold to the Fund, payable in gold, shall be levied against the country selling its blocked balances and against the country in which the balances are held. In addition a charge of not less than one percent, payable in gold, shall be levied annually against each country on the amount of such balances remaining to be purchased by it.

(*e*) If the country selling blocked balances to the Fund asks for foreign exchange rather than local currency, the request will not be granted unless the country needs the foreign exchange for the purpose of meeting an adverse balance of payments not arising from the acquisition of gold, the accumulation of foreign balances, or other capital transactions.

(*f*) Either country may, at its option, increase the amount it repurchases annually. But, in the case of the country selling blocked balances to the Fund, not more than 2 percent per annum of the original sum taken over by the Fund shall become free, and only after 3 years shall have elapsed since the sale of the balances to the Fund.

(*g*) The Fund has the privilege of disposing of any of its holdings of blocked balances as free funds after the 23-year period is passed, or sooner under the following conditions:

  (i) Its holdings of the free funds of the country in which the balances are held fall below 20 percent of its quota; or

  (ii) The approval is obtained of the country in which the balances are held.

(*h*) The country in which the blocked balances are held agrees not to impose any restrictions on the use of the installments of the 40 percent portion gradually repurchased by the country which sold the balances to the Fund.

(*i*) The Fund agrees not to sell the blocked balances acquired under the above authority, except with the permission or at the request of the country in which the balances are being held. The Fund may invest these balances in the ordinary or special government securities of that country. The Fund shall be free to sell such securities in any country under the provisions of V–11, below.

(*j*) The Fund shall determine from time to time the maximum proportion of the blocked balances it will purchase under this provision.

Provided, however, that during the first 2 years of its operation, blocked balances purchased by the Fund shall not exceed in the aggregate 10 percent of the quotas of all member ccountries. At the end of 2 years of operation, the Fund shall propose a plan for the gradual further liquidation of blocked balances still outstanding indicating the proportion of the blocked balances which the Board considers the Fund can appropriately purchase.

Blocked balances acquired under this provision shall not be included either in computing the amount of foreign exchange available to member countries under their quotas (cf. V–2, 3), or in computing charges on balances of local currency in excess of the quotas (cf. V–14).

9. To buy and sell currencies of non-member countries but shall not acquire more than $10 million of the currency of any one non-member country nor hold such currencies beyond 60 days after date of purchase except with the approval of the Board.

10. To borrow the currency of any member country provided the additional amount is needed by the Fund and provided the representative of that country approves.

11. To sell member-country obligations owned by the Fund provided that the representatives of the country issuing the securities and of the country in which the securities are to be sold approve, except that the approval of the representative of the issuing country shall not be necessary if the obligations are to be sold in its own market.

To use its holdings to obtain rediscounts or advances from the Central Bank of any country whose currency the Fund needs.

12. To invest any of its currency holdings in government securities of the country of that currency provided that the representative of the country approves.

13. To lend to any member country its local currency from the Fund for 1 year or less up to 75 percent of the currency of that country held by the Fund, provided the local currency holdings of the Fund are not reduced below 20 percent of the quota.

14. To make a service charge on all gold and exchange transactions.

To levy a charge uniform to all countries, at a rate not less than 1 percent per annum, payable in gold, against any country on the amount of its currency held by the Fund in excess of the quota of that country. An additional charge, payable in gold, shall be levied by the Fund against any member country on the Fund's holdings of its currency in excess of the permissible quota of that country.

In case the Fund finds it necessary to borrow currency to meet the demands of its members, an additional charge, payable in gold, shall be made by the Fund sufficient to cover the cost of the borrowing.

15. To levy upon member countries a *pro rata* share of the expenses of operating the Fund, payable in local currency, not to exceed one-tenth percent per annum of the quota of each country. The levy may be made only to the extent that the earnings of the Fund are inadequate to meet its current expenses.

16. The Fund shall deal only with or through:

(*a*) The Treasuries, Stabilization Funds, or Central Banks acting as fiscal agents of member governments.

(*b*) Any international banks owned predominantly by member governments.

The Fund may, nevertheless, with the approval of the representatives of the governments of the countries concerned, sell its own securities, or securities it holds, directly to the public or to institutions of member countries.

VI. Management

1. The administration of the Fund shall be vested in a Board of Directors. Each government shall appoint a director and an alternate, in a manner determined by it, who shall serve for a period of 5 years, subject to the pleasure of their government. Directors and alternates may be reappointed.

2. In all voting by the Board, the director or alternate of each member country shall be entitled to cast an agreed upon number of votes.

The distribution of *basic votes* shall be closely related to the quotas of member countries, although not in precise proportion to the quotas. An appropriate distribution of basic voting power would seem to be the following: Each country shall have 100 votes, plus 1 vote for the equivalent of each 100,000 unitas ($1 million) of its quota.

No country shall be entitled to cast more than one-fifth of the aggregate basic votes, regardless of its quota.

3. All voting shall be according to basic votes except as follows:

(*a*) In voting on proposals to authorize the sale of foreign exchange, each country shall cast a number of votes modified from its basic vote:

   (i) By the addition of one vote for each $2 million of net sales of its currency by the Fund (adjusted for its net transactions in gold), and

   (ii) By the subtraction of one vote for each $2 million of its net purchases of foreign exchange from the Fund (adjusted for its net transactions in gold).

(*b*) In voting on proposals to suspend or restore membership, each member country shall cast one vote, as provided in VI–11, below.

4. All decisions, except where specifically provided otherwise, shall be made by a majority of the member votes.

5. The Board of Directors shall select a Managing Director of the Fund and one or more assistants. The Managing Director shall become an *ex officio* member of the Board and shall be chief of the operating staff of the Fund. The operating staff shall be selected in accordance with regulations established by the Board of Directors.

6. The Board of Directors shall appoint from among its members an Executive Committee of not less than 11 members. The Chairman of the Board shall be Chairman of the Executive Committee, and the Managing Director of the Fund shall be an *ex officio* member of the Executive Committee.

The Executive Committee shall be continuously available at the head office of the Fund and shall exercise the authority delegated to it by the Board. In the absence of any member of the Executive Committee, his alternate shall act in his place. Members of the Executive Committee shall receive appropriate remuneration.

7. The Board of Directors may appoint such other committees as it finds necessary for the work of the Fund. It may also appoint advisory committees chosen wholly or partially from persons not employed by the Fund.

8. The Board of Directors may at any meeting authorize any officers or committees of the Fund to exercise any specified powers of the Board not requiring more than a majority vote.

The Board may delegate any authority to the Executive Committee, provided that the delegation of powers requiring more than a majority of the member votes can be authorized only by a majority (of the Board) of the same size as specified, and can be exercised by the Executive Committee only by like majority.

Delegated powers shall be exercised only until the next meeting of the Board, and in a manner consistent with the general policies and practices of the Board.

9. The Board of Directors may establish procedural regulations governing the operations of the Fund. The officers and committees of the Fund shall be bound by such regulations.

10. The Board of Directors shall hold an annual meeting and such other meetings as it may be desirable to convene. The annual meeting shall be held in places designated by the Executive Committee, but not more than one annual meeting in any 5-year period shall be held within the same member country.

On request of member countries casting one-fourth of the votes, the Chairman shall call a meeting of the Board for the purpose of considering any matters placed before it.

11. A country failing to meet its obligations to the Fund may be suspended provided a majority of the member countries so decides. While under suspension, the country shall be denied the privileges of membership but shall be subject to the same obligations as any other member of the Fund. At the end of 1 year the country shall be automatically dropped from membership unless it has been restored to good standing by a majority of the member countries.

Any country may withdraw from the Fund by giving notice, and its withdrawal will take effect 1 year from the date of such notice. During the interval between notice of withdrawal and the taking effect of the notice, such country shall be subject to the same obligations as any other member of the Fund.

A country which is dropped or which withdraws from the Fund shall have returned to it an amount in its own currency equal to its contributed quota, plus other obligations of the Fund to the country, and minus any sum owed by that country to the Fund. Any losses of the Fund may be deducted *pro rata* from the contributed quota to be returned to the country that has been dropped or has withdrawn from membership. Local currency holdings of the Fund in excess of the above shall be repurchased by that country with gold or foreign exchange acceptable to the Fund.

When any country is dropped or withdraws from membership, the rights of the Fund shall be fully safeguarded. The obligations of a country to the Fund shall become due at the time it is dropped or withdraws from membership; but the Fund shall have 5 years within which to liquidate its obligations to such country.

12. Net profits earned by the Fund shall be distributed in the following manner:

(*a*) Fifty percent to reserves until the reserves are equal to 10 percent of the aggregate quotas of the Fund.

(*b*) Fifty percent to be divided each year among the members in proportion to their quotas. Dividends distributed to each country shall be paid in its own currency or in gold at the discretion of the Fund.

VII. Policies of Member Countries

Each member country of the Fund undertakes the following:

1. To maintain by appropriate action exchange rates established by the Fund on the currencies of other countries, and not to alter exchange rates except as provided in IV–5, above.

Exchange rates of member countries may be permitted to fluctuate within the specified range fixed by the Fund.

2. Not to engage in exchange dealings with member or non-member countries that will undermine stability of exchange rates established by the Fund.

3. To abandon, as soon as the member country decides that conditions permit, all restrictions (other than those involving capital transfers) over foreign exchange transactions with other member countries, and not to impose any additional restrictions (except upon capital transfers) without the approval of the Fund.

The Fund may make representations to member countries that conditions are favorable for the abandonment of restrictions over foreign exchange transactions, and each member country shall give consideration to such representations.

All member countries agree that all of the local currency holdings of the Fund shall be free from any restrictions as to their use. This provision does not apply to blocked foreign balances acquired by the Fund in accordance with the provisions of V–8, above.

4. To cooperate effectively with other member countries when such countries, with the approval of the Fund, adopt or continue controls for the purpose of regulating international movements of capital. Cooperation shall include, upon recommendation by the Fund, measures that can appropriately be taken, such as:

(*a*) Not to accept or permit acquisition of deposits, securities, or investments by nationals of any member country imposing restrictions on the export of capital except with the permission of the government of that country and the Fund;

(*b*) To make available to the Fund or to the government of any member country such information as the Fund considers necessary on property in the form of deposits, securities and investments of the nationals of the member country imposing the restrictions.

5. Not to enter upon any new bilateral clearing arrangements, nor engage in multiple currency practices, which in the judgment of the Fund would retard the growth of world trade or the international flow of productive capital.

6. To give consideration to the views of the Fund on any existing or proposed monetary or economic policy, the effect of which would be to bring about sooner or later a serious disequilibrium in the balance of payments of other countries.

7. To furnish the Fund with all information it needs for its operations and to furnish such reports as the Fund may require in the form and at the times requested by the Fund.

8. To adopt appropriate legislation or decrees to carry out its undertakings to the Fund.