The Future of the International Monetary System

I. Introduction

I shall not try to *forecast* this future; for if I yielded to that wish, and projected recent trends into the months or years immediately ahead, I could only tell that the international monetary system *has no future*, because our political leaders — and, alas, their economic advisers! — may be unable to muster the lucidity and the courage required to negotiate and implement the radical, agonizing, reforms indispensable to cure the world inflation, recession, balance-of-payments disequilibria, chaotic exchange-rate fluctuations, creeping protectionism etc., to which we seem to be condemned.

I prefer to concentrate on *what should be done to reverse the process*, even if the chances are that nothing of the kind will be done in the foreseeable future. I would rather run one chance out of ten to help build a better future than nine chances out of ten to predict correctly the disasters that may await us.

Advice about institutional reforms, however, must be based on a clear understanding of the major shortcomings of the present institutions. Many of my economic colleagues, particularly in the United States and in England, became increasingly convinced, a few years ago, that a major portion of the blame could be placed on the system of fixed, even though adjustable, exchange rates enshrined in the Bretton Woods system. The experience of the last six or eight years has disabused most of us of the illusion that floating rates would lessen inflation rates, unemployment, and balance-of-payments disequilibria. A few may still hold consistently, however, that the growing inflation, unemployment and balance-of-payments disequilibria of the floating rates regime are due to the fact that governments do not let them float freely, under the impact of market supply and demand, but insist on continued interventions and management — or rather mismanagement? — by the official authorities. Others — and I con-

fess to be among them — hold that some amount of concerted *international* management would be less harmful than either freely floating or nationally managed rates.

My major thesis, however, is that neither stable, nor floating, exchange rates can function satisfactorily in the absence of any international control, and *restraints*, over the fantastic explosion of international liquidity provided to the market, in recent years, by the monetary authorities and the commercial banking system. In developing this thesis, I shall center on the *inflationary* aspects of this phenomenon, and neglect — regrettably — the problems of recession and unemployment, which I certainly regard as an even worse ill than inflation, but to which inflation has proved, I think, to be a contributing factor rather than an effective and lasting remedy.

II. The Main Monetary Source of the World Inflation

Admittedly, the root causes of the world inflation in which we are now engulfed lie outside the field of monetary policies and institutions, national or international. The unprecedented growth of material production, and consumption, initiated some 200 years ago by the *industrial revolution* undoubtedly helped meet real needs for food, shelter, health, transportation, etc., and remains essential to the attainment of decent health and living standards in the poorer, less developed countries. It was later sustained and accelerated, however, first by the *advertising revolution* which created new needs unperceived before, secondly by the *Keynesian revolution* which warded off in the postwar years the cyclical recessions which previously interrupted or reversed periodicallly the growth process, and, thirdly, by the fantastic explosion of *military expenditures* to a level of $400 billion to $500 billion a year, just about equal to the total G.N.P. of China, Bangladesh, and India, double that of the thirty other poorest countries, and two thirds of that on which 36 countries grouping 57% of the world's population have to live or to starve.[1]

These non-monetary factors are the basic roots of the world inflation. They have brought within our horizon increasing scarcities

[1] On less than $ 260 a year (0,71 U.S. cents per day) in 1976, i.e. about 2.8% of the per capita G.N.P. of Switzerland, 3.3% of that of U.S., and 3.7% that of Belgium. These calculations are derived from the estimates of the *1978 World Bank Atlas.*

of essential foods and raw materials, and environmental problems, which can be overcome only by huge investments and rising costs of production. These latter are further accelerated by collective bargaining and pressure groups, and spread from the scarce sectors to the others.

It is at this point that monetary policies enter the inflationary process. They may accomodate it by expanding bank credit to the official and private sectors of the economy, thus financing increases in wage, costs, and prices; or they may refuse such financing, but at the risk of slowing down not only inflation, but economic activity itself, at least temporarily.

The evolution of the national monetary systems and of the international monetary system itself has tended, over the years, to eliminate former constraints on the inflationary proclivities to be expected from both the public and the private sectors of the economy. This, I believe, is the crucial issue in the acceleration of national and international inflation since the first and the second world wars, and particularly at the present juncture. Obvious as it may be, it deserves more emphasis from the economic profession.

Gold was traditionally the major constraint on such proclivities, but its beneficial role in this respect has been vastly exaggerated by the enthusiasts of the gold standard. Credit money — i.e. bank currency and deposits — played an overwhelming part in sustaining feasible rates of economic growth in the century before the first world war. By 1913 already, credit money accounted for about 85 per cent of estimated — or "guesstimated" — world money supply,[2] and its widespread use did not prove incompatible with a closer approach to non-inflationary rates of monetary expansion than in the previous gold and silver money regimes, subject to repeated debasements of the coinage. Any country determined to fight inflation would be better advised to try legal, or constitutional, ceilings on money creation (x per cent a year, for instance, *à la* Milton Friedman) than to tie money creation to gold. I shall abstain from pursuing this suggestion any further, and turn instead to my main topic, *i.e.* the *international* monetary system.

The major development here is, without question, the generalization after the first, and particularly after the second, world war of the

[2] See table 1, p. 62, of my Princeton Study on *The Evolution of the International Monetary System: Historical Reappraisal and Future Perspectives*, Princeton 1964.

so-called gold exchange standard, under which all but one or a few countries accumulated their international monetary reserves not only in gold, but more and more in one or a few *national*, so-called "reserve currencies" — primarily sterling at first, and later the U.S. dollar — legally convertible into gold upon single request by their holders. I pointed out long ago[3] that the inflationary proclivities of such a system made its breakdown inevitable. The gold convertibility of the sterling standard had had to be suspended in 1931, and that of the mightier dollar standard collapsed similarly in 1971.

Most of the academic and official debates concerning the recent evolution of our international monetary system have unfortunately centered on two secondary issues, rather than on the most crucial one:

1) The explosion of oil prices, which occurred only in the last months of 1973, and cannot therefore be blamed for the suspension of the dollar convertibility in 1971, nor for the doubling of world reserves over the years 1970-1972.

2) The merits and demerits of floating *vs* stable (but adjustable) exchange rates. Interesting as it is, this debate obscures the fact that world reserves have grown, under both systems, at a wildly inflationary rate incompatible with the proper functioning of either.

3) Far more significant is the inflationary proclivity of any reserve-currency standard — convertible as well as inconvertible — enabling the reserve-currency center to finance huge and persistent deficits — internal as well as external — by the flooding of world reserves with its own *IOU's*.

Not to drown the reader in an ocean of statistical estimates, let me merely mention the highlights of world reserve creation in the last six years (1973-1978) of the floating exchange rates regime under which we live today. Measured in dollars, at current market prices, world reserves have tripled over these six years, increasing by $ 380 billion, from $ 191 billion to $ 571 billion, at an average pace of 20%

[3] In 1957 in my book *Europe and the Money Muddle*, and in greater detail in two papers in the March and June 1959 issues of this *Review* («The Return to Convertibility: 1926-1931 and 1958-? Or Convertibility and the Morning After" and "Tomorrow's Convertibility: Aims and Means of International Monetary Policy") and in my 1960 *Gold and the Dollar Crisis*.

per year, multiple of course of any fleasible growth in world trade and production in real terms.

What are the sources of this increase?

1) World physical monetary gold holdings, measured in SDR's (or in ounces) contributed less than nothing to it. Indeed, they declined slightly as a result of official sales to the private market by the IMF and the United States.

2) There were no SDR allocations over this period. (Their resumption in 1979 is unlikely to account for more than 3% of reserve increases this year.)

3) Net IMF credits contributed about 2%.

4) The remaining *98%* were derived from the two following sources:

a) 33% from Central Banks' accumulation of *national* currencies (overwhelmingly dollars and Euro-dollars) as *international* reserves, *i.e.* to the financing of a few rich countries, primarily the United States;

b) 65% (nearly two thirds) from the rise of gold market prices measured in SDR's (34%) and from the rise of the SDR itself vis-à-vis the U.S. dollar (31%).[4]

A major portion of these reserve increases valued in dollars undoubtedly reflects bookkeeping profits rather than acquisition costs, — and *realized inflationary impact* — of reserves accumulated in the past by the monetary authorities, and to which SDR-valued reserve increases of 133 billion provide a closer, although very imperfect approximation. These bookkeeping profits will, however, be passed on sooner or later to Governments, and are practically certain to elicit in many countries more expansionist fiscal and monetary policies *in the future* than would have been the case otherwise.

[4] Soaring gold prices were the major source (82%) of a further $ 58 billion increase of world reserves in the first five months of 1979. Revaluing the end of May reserves at the October 1st London price of $ 414.75 per ounce would account for 97% of a total increase of world reserves by $ 218 billion since the end of 1978 to $ 787 billion.

TABLE I

SOURCES OF OFFICIAL RESERVE CREATION
(in billions of SDR's at 35 per ounce, and of U.S. dollars)

	End of			1973-June 1979 Increases		Ratios: June 79/ Dec. 72
	1972	1978	June 1979	in billions of SDR's or $	in % of Total $ Increase	
A. *In billions of SDR's*	**147**	**279**	**291**	**144**	**32**	**1.98**
I. World Gold	*41*	*40*	*40*	*—2*	*—*	*0.96*
II. International Credit	*105*	*239*	*251*	*146*	*33*	*2.38*
A. Foreign Exchange	96	221	230	134	30	2.40
B. SDR Allocations	9	9	13	4	1	1.43
C. Net IMF Credit	—	9	8	8	2	9.07
B. *Impact of Valuation Changes*	**44**	**291**	**348**	**304**	**68**	**7.87**
I. Of SDR gold price on gold valuation	*29*	*159*	*204*	*175*	*39*	*6.99*
II. Of $ price of SDR on:	*15*	*133*	*144*	*129*	*29*	*9.55*
A. Gold valuation in $	6	60	71	65	14	11.76
B. International credit in $	9	72	73	64	14	8.07
C. *Total (A+B) Reserves in billions of dollars*	**191**	**571**	**639**	**448**	**100**	**3.35**
I. World Gold	76	259	315	238	53	4.12
II. International Credit	114	312	324	210	47	2.83

Sources and Notes: See Appendix Table 1

Reserve investments in the United States (mostly in Treasury securities and bank deposits) account for the major portion of world foreign exchange reserves, and of their growth. Direct and indirect (through U.S. banks' branches abroad) U.S. liabilities to foreign official holders, as reported in the *Federal Reserve Bulletin*, total more than two thirds of these reserves, both in 1972 and in 1978, the remainder being accounted in part (about 12%) by Euro-dollar creation by foreign banks, and in part (about 20% of the total, according to IMF sample estimates) by other foreign currencies: marks, Swiss francs etc. Few economists are probably aware of the full inflationary impact of this financing upon the rest of the world.

The first — and most widely understood — is that it gave the U.S., under floating as well as under fixed rates, what de Gaulle called the "extravagant privilege" of financing most of our deficits with our own

IOU's. The reported direct and indirect liabilities of the U.S. to foreign official holders totalled $ 194 billion at the end of 1978, *i.e.* nearly 15 times our total reserve assets of $ 13 billion at the end of 1972. Their increase of $ 124 billion (from $ 70 billion at the end of 1972) was of course the main feeder of huge, persistent and increasing deficits which we would have been unable to sustain if we had had — like other countries — to finance them from our own reserves.[5]

TABLE II

COMPOSITION OF WORLD FOREIGN EXCHANGE RESERVES: 1972-1978
(in billion of $, and in per cents of total)

	End of		1973-1978 Increases	% of Total	
	1972	1978		1972	1978
I. *U.S. Liabilities*	**70**	**194**	**124**	**67**	**67**
A. Direct	62	162	100	60	56
B. Foreign Branches of UMSM Banks	8	32	24	8	11
II. *Other* (III-I)	**34**	**94**	**60**	**33**	**33**
A. Other currencies	21	58	37	20	20
B. Euro-dollars (other than IB)	13	36	23	13	13
III. *Total Foreign Exchange Reserves*	**104**	**288**	**184**	**100**	**100**

Sources and Notes:
I. *U.S. Liabilities:* Tables 3.14 and 3.13 of *Federal Reserve Bulletin*.
II. A. *Other Currencies:* Rough estimates of 20% of total foreign exchange reserves (Line III), based on sample estimates published in *IMF Survey*, May 22, 1978, p. 155.
Lines II and IIB are obtained residually: II = III-I and IIB = II-IIA (Line II B Euro-dollar estimate of $ 13 billion in 1972 corresponds closely to the estimate of "identified Eurodollars" reported in the *IMF Annual Report 1978*, p. 53, converted into dollars, *minus* I B).
III. *Total Foreign Exchange Reserves: International Financial Statistics*, August 1979, p. 32 estimates, converted from SDR's into $'s.

What is less understood is that the combination of floating exchange rates with the flooding of world reserves by paper claims on a few reserve centers has also suppressed a major restraint on domestic inflationary policies by all countries alike. As long as world reserve increases remained moderate — *i.e.* until the end of the 1960's — domestic inflationary policies were sanctioned by balance-of-payments de-

[5] Note, however, that this increased indebtedness to foreign official holders financed the "recycling" role of the dollar, imposed upon U.S. by its reserve-currency use, rather than the current account deficits of the U.S. itself. Net capital exports over these six years, as reported by the *Survey of Current Business* (June 1979), totalled $ 135 billion, of which $ 24 billion were financed by *surpluses* on goods, services and remittances, and $ 111 billion by increased U.S. liabilities to foreign official holders. See Annex Table 3.

ficits and reserve losses, entailing fairly rapidly the inability of the more inflationary countries to avoid a devaluation, or depreciation, of their currency. This was a traumatic experience, especially under a legal system of fixed rates, since it involved an obvious failure of official policies, exposing responsible officials to the danger of not being retained, reappointed or reelected to their job. Daily floating rates have greatly weakened this trauma and its consequent *political* deterrent to persistent inflationary policies. Floating rates speed up the readjustment of exchange rates to competitive levels by the more inflationary countries, but tend also to facilitate the continued pursuit of inflationary policies by them.

Concern about the domestic and external impacts of inflationary policies has not vanished. It has indeed increased with the acceleration of inflation, but the most effective — *because unavoidable* — barrier to them has practically disappeared. The United States was not restrained by gross reserve losses, because the acceptance of its own currency — which it can produce without limit — by other countries enabled it to finance enormous deficits, before and even after the dollar became inconvertible. What is less perceived so far in most of our economic debates is that the size and persistence of these deficits, together with floating exchange rates, have practically eliminated any substantial losses of reserves, even by the most inflationary countries. Significant reserve losses were experienced by about a dozen countries only in the first years following the explosion of oil prices, but gross reserves, even expressed in SDR's rather than in dollars, and with gold valued throughout at 35 SDR's per ounce, more than doubled on the average, for countries other than the United States and the oil-exporting countries over the three years 1970-1972, and have nearly doubled again (a 75 per cent increase) since 1972. Even the non-oil exporting less developed countries increased their reserves by 65 per cent from 1969 through 1972, and by 168 per cent in the following six years. Reserve declines of more than 50 million SDR's are reported by *International Financial Statistics* (in its annual 1979 issue) for only two countries other than the United States from 1969 through 1972[6] and nine countries over the following six years.[7]

[6] Zambia and, curiously, South Africa, with losses of SDR 200 million each.

[7] Losses of SDR 3,800 million are reported for Australia, 2,065 million for Canada, 685 million for Portugal, 523 million for Turkey, 521 million for South Africa, 420 million for New Zealand, 107 million for Zambia, 106 million for Jamaica, and 51 million for Greece.

This does not mean, of course, that all other countries were in surplus on current account, but merely that the current account deficits of even the most inflationary ones could be financed — and indeed overfinanced — by international borrowing.

The flooding of world reserves by dollar and Euro-dollar creation has added new dimensions to this financing. It has increased the cash reserves of commercial banks, enabling them to expand their own foreign lending at a pace which they could not have sustained otherwise. I shall come back to this problem in the concluding pages of this paper, but must first explain why I still retain some hope of reviving the drive for world monetary reform, more indispensable today than ever, but which harassed officials practically abdicated in Jamaica and the Second IMF Amendment. "I am not optimistic", Jean Monnet used to say, "I am persistent".

TABLE III

GEOGRAPHICAL DISTRIBUTION OF WORLD RESERVES: 1969-1972

	End of year, in SDR billions			Ratios		
	1969	1972	1978	1972/1969	1978/1972	1978/1969
World	79	147	278	1.86	1.91	3.55
United States	17	12	15	0.71	1.24	0.88
Other Countries:	62	134	264	2.18	1.97	4.29
OPEC	4	10	46	2.45	4.62	11.27
Other Countries	58	124	218	2.16	1.75	3.79
Developed	46	105	165	2.30	1.58	3.62
Less developed	12	20	53	1.65	2.68	4.42

Source: International Financial Statistics, Annual 1979 (pp. 45 and 47)

III. Resuming the Aborted Drive toward Indispensable Reforms

1. The EMS Breakthrough

The most hopeful sign of possible progress toward reform, since the breakdown of the Bretton Woods System, is the breakthrough finally achieved in March 1979 with the initiation of the *European Monetary System* (EMS for short).

I shall not dwell here on this topic, limiting myself to a few observations necessary to dispel widespread misunderstandings about the aims and mechanics of the EMS.[8]

The scepticism — and often downright opposition — of many American economists to this new and crucial development is primarily inspired by the conviction that commitments to exchange-rate stability are premature, harmful, and bound to fail, as long as the participating countries do not succeed in reducing the wide divergences still prevalent today between their national rates of inflation.[9] What they fail to understand is that this conviction is fully shared by the EMS negotiators themselves and that the new system aims indeed to accelerate, rather than prevent, the exchange-rate readjustments still expected to be inevitable in the years immediately ahead. Full monetary union — and even irrevocable commitments to exchange-rate stability — is only a hope, still relegated to the future and conditional upon the harmonization, hopefully downward, of inflation rates and the consolidation of this harmonization through ambitious reforms, not yet fully agreed or even formulated, transferring adequate jurisdiction from national to Community authorities and institutions.

Let me mention briefly three crucial features of the system most attractive to its promoters.

1) The system restores for the participating currencies, a *common denominator* — or numéraire — sadly lacking in the reformed IMF Agreement. This common denominator is the ECU, defined as a weighted basket of the participating currencies. Unsatisfactory as this definition may be, it is a more realistic benchmark for exchange-rate calculations, readjustments, and progress toward stability than

[8] For further details, see my suggestions for "The American Response to EMS" in *The European Monetary System: Its Promise and Prospects* (Philip H. Trezise, Editor, The Brookings Institution), from which I have extracted here a few relevant passages.

[9] Professor Brunner's criticism in the December 1979 issue of this *Review* ("Reflections on the State of International Monetary Policy") is more subtle. He dismisses as "hardly workable" the "orchestrated construction" of a EMS anchored on the ECU, but as "politically unpalatable" the "simple and workable" solution of a "hegemonial system with appropriate adjustments to the policy of the hegemonial authority". His preferred "hegemonial" currency would presumably be the German mark rather than the dollar whose mismanagement spelled the breakdown of the Bretton Woods system. Slow and difficult as it will be to implement, the EMS "orchestrated construction" still seems to me, therefore, politically inescapable, and preferable economically as well as politically to the disorderly chaos to which Professor Brunner appears to be resigned.

a widely fluctuating dollar, since trade, services, and capital transactions among the countries of the European Community and others — in Western Europe, the Middle East and Africa — likely to gravitate around the ECU encompass two-thirds to three-fourths of their total external transactions, *i.e.* close to ten times their transactions with the United States (see Annex Table 4).[10]

2) One of the first consequences of this definition is to give, for the first time, an *operational* significance to the principle formulated in Article 107 of the Rome Treaty: "Each Member State shall treat its policy with regard to rates of exchange as a matter of common concern". Since each country's official rate is defined in terms of the ECU, and since the ECU itself is defined as a weighted *average* of member currencies, it is impossible for any one currency to revalue upward — or downward — in terms of this *average* without a compensatory depreciation — or appreciation — of all the other participating currencies. Any readjustment of mutually agreed exchange rates can thus be effected only by mutual consent.[11]

3) Two other exchange-rate commitments are also central to the EMS agreement. The first is taken from the former "snake" agreement: the monetary authorities of each country are committed to intervene in the exchange market — through sales or purchases of their own currency — in order to limit bilateral exchange fluctuations between their currency and any other participating currency to a 2.25% margin (temporarily enlarged to 6% for Italy). The second, and totally novel one, is to calculate for each currency a so-called "*divergence indicator*" reflecting its market fluctuations in terms of the ECU vis-à-vis its officially agreed central ECU rate. When these fluctuations reach a certain percentage of the maximum divergence possible under the bilateral margins system, the monetary authorities of the

[10] One may argue that the somewhat larger shares of total trade contractually denominated in $ are more relevant, but the choice of the $ denomination in transactions with countries other than the U.S. is itself an illogical residue of past habits, no longer justified today.

[11] As demonstrated by the first readjustment of this sort — and certainly not the last on September 24, 1979. Note, however, that readjustments were first calculated on a *bilateral* basis, as before (an upvaluation of the D.M. by 5% against the Danish Krone and 2% against each of the other six participating currencies, with no change in the bilateral rates between the latter), and the implied rates vis-à-vis the ECU derived afterwards and entailing an upvaluation of the DM by 1.01%, a devaluation of the Krone by 3.8% and a uniform 0.97% devaluation of the other six currencies. (The fictitious central rate of the British Pound vis-à-vis the ECU was readjusted also on this occasion by - 2.07%).

issuing country are automatically presumed to take appropriate action (market interventions, internal monetary policy measures and or other economic policy measures, and/or readjustment of its central rate vis-à-vis the ECU), or, if they fail to take action, to explain and discuss with their partners the ways in which the situation should be corrected. Thus, in total contrast with Bretton Woods and all other traditional monetary "sovereignty" rules, consultations on desirable exchange-rate readjustments may be forced upon a reluctant country, rather than left exclusively to its own initiative.

4) Beyond its "numéraire" and "divergence indicator" functions, the ECU also serves not only as a unit-of-account for an increasing number of Community transactions, but also as a real money of settlement and reserve accumulation.

Central bank stabilization interventions in the exchange market should be conducted, as far as possible, in member currencies rather than in dollars. Since, however, central banks do not in principle accumulate member currencies as reserves, such interventions require mutual credit operations between the two central banks concerned, the issuing bank of the strong currency accumulating claims against the issuing bank of the weak currency. Central banks grant each other through the EMCF (European Monetary Cooperation Fund) *unlimited* very short-term financing for their interventions and short-term monetary support, which can be supplemented further by medium-term financial assistance, granted by the Council under appropriate conditions. These short and medium-term arrangements now entail lending commitments totalling in theory 38.7 billions of ECU, but not all of which could in fact be simultaneously utilized.

The borrower can exercise one of several options, or combination of options, when the reimbursement falls due. In case he wishes to settle in ECU's, he cannot force upon a reluctant creditor ECU settlements exceeding 50% of the amount due. For any portion not settled in ECU's, the general rule — in the absence of any other agreement between the two parties — is to settle in reserve components in the same proportions as those in which the debtor central banks holds its reserves, gold, however, being excluded. In practice, therefore, the option is primarily between ECU or dollar repayments.

But how do central banks acquire such ECU's? They are credited in ECU accounts on the books of the EMCF against equivalent transfers[12] of gold and dollar reserves for amounts equal to 20% of each country's gold and dollar assets. The conversion of these gold and dollar transfers into ECU's takes place at current or (for gold) average market prices over the preceding six months. They totalled initially, last June, about 26 billions of ECU's, *i.e.* about $ 35 billions, and ECU 29 billion, equivalent to nearly $ 40 billion at the end of September.

The EMS baby is only six months old, but is deemed by its parents to be reasonably healthy. Its growth to adulthood, however, will require additional and crucial agreements calling for a high degree of political vision and responsibility. I wish I could review here, in particular, the steps necessary to transform the EMCF into a European Monetary Fund, and, later on, into the Federal Reserve System of a full-fledged Monetary Union. This, however, deserves another paper.

Here I shall consider the external — rather than internal — problems confronting the EMS, in the immediate and longer-run future.

2. *The ECU and the Dollar*

One of the first and most urgent problems confronting non-member countries as well as member countries is the insertion of the EMS into the world monetary system, and particularly the uneasy relationship between the ECU and the dollar in international settlements.

An important feature of the EMS in this respect is highly welcome by our monetary authorities. This is the *replacement* — in principle at least — of the dollar by Community currencies in intra-Community interventions on the exchange market and by the ECU in the settlement of mutual credits. We have often, and justifiably, complained of the dominant use of the dollar in both of these respects, as it could exercise strong — even though unintended — upward or downward pressures on dollar exchange-rates, irrespective of any development in the dollar competitiveness in world trade, whenever Community countries' surpluses or deficits switch from eager to reluctant dollar holders, or vice-versa.

[12] These "transfers", however, are still *for the moment* reflected in renewable three months' *swaps*, leaving the exchange risks on gold and dollars to the depositing central bank rather than sharing them through the EMCF.

The first months of functioning of the EMS have been somewhat disappointing in this respect, dollar interventions having remained far larger so far than was intended. New measures are now under discussion to make possible a further reduction in the use of the dollar in market interventions and settlements. If successful, these measures should eliminate unnecessary pressures — upward or downward — on the dollar rate, and restore the disciplines whose excessive relaxation has proved — as discussed above — the major engine of world inflation and continued balance-of-payments disequilibria for other countries as well as for the United States.

The use of the ECU outside the Community itself might, at first view, be more worrisome. As mentioned already, the ECU is likely to provide a powerful pole of attraction for other European, Middle East and African countries for which the Community accounts for a major portion of their total trade. Some of these countries are already looking in fact to the ECU as a potential benchmark for their exchange-rate policies and stabilization endeavors. Switches from dollars to ECU's in private and official settlements and reserve accumulation might become very tempting, if made possible by the EMS authorities, or by the imaginative Euro-currency and Euro-bond sectors of the world economy. Such switches might depress dollar rates unduly on the exchange markets, if not effected — as suggested below — with the EMF instead.

A close, two-way, cooperation between the EMS and the U.S. authorities will be necessary, in any case, to prevent a further weakening of an already undervalued, overcompetitive dollar. If this trend were allowed to proceed much further, it would inevitably trigger protectionist reactions abroad against so-called "foreign exchange dumping" by the U.S., and possibly panicky reactions in the United States itself.

The fear of such a disastrous course of events is a powerful stimulus to cooperation between the U.S. and Europe, and the EMS provides new and unprecedented instruments to make such cooperation more feasible and effective than in the past.

The first requirement in this respect will be the correction of the huge and growing U.S. deficits of recent years, and indeed the restoration of healthy surpluses in the balance of payments on current account. This, in turn, will require an even more determined and successful fight to reduce the profligate American oil consumption and imports and the rate of domestic inflation double or triple that of

Germany, Japan, Belgium, the Netherlands, or Austria, to say nothing of Switzerland. The clear affirmation of these prior policy objectives by the Congress as well as by the Administration, and their early implementation by concrete restraints on fiscal overspending, excessive money creation, price and wage increases, oil consumption and imports, etc. should help restore confidence in the dollar, and reverse bearish speculation against it by Americans and by foreigners.

Yet a total and lasting correction of the U.S. deficits cannot be expected overnight. Corrective policies — including past readjustments of the exchange rates — produce their effects only slowly. The avoidance of an excessive depreciation of the dollar will still require considerable financing of tapering-off foreign deficits for some time to come.

The U.S. can, first of all, draw for this purpose on its own international reserves, estimated at $ 18 billion at the end of October, but which would approximate in fact $ 200 billion if gold holdings were revalued at the current price of gold on the market. This latter estimate would, of course, be excessive since gold prices would collapse in the event of *massive* sales from our reserves. It is relevant, however, as one of the many reassurances to prospective creditors about our solvency, and as an indication of our ability to transfer gold at — or close to — market prices *to foreign monetary authorities* in settlement of their dollar claims.

Far more important, of course, is the willingness, amply demonstrated already, of foreign countries to participate in a joint defense of agreed dollar rates, including the readjustments — upward as well as downward — that might be deemed appropriate, or unavoidable, before any stabilization of the dollar vis-à-vis the other major currencies can be realistically envisaged, even as a *presumptive* goal rather than a legally binding commitment. The radical policy changes announced and put into operation since November 1978 — and reinforced on October 6, 1979 — are essential in this respect.

We have, first of all, accepted to intervene massively in the exchange market, rather than leave such interventions nearly exclusively to others. We have, secondly, agreed to reduce the inflationary impact of our borrowing abroad by borrowing in the financial market, rather than nearly exclusively from central banks. Thirdly, we are now ready to denominate our foreign borrowings in the creditors' currencies as well as in our own, in order to make them more attrac-

tive and acceptable to prospective lenders deterred by the risk of exchange losses on a depreciating dollar. Fourthly, we are now willing to explore actively with our IMF partners the opening of so-called "substitution accounts" in SDR's as a way to mop up some of the dollar overhang accumulated in the past.[13]

The EMS opens up new opportunities in all of these respects.

First of all, the adoption of the ECU as a parallel currency may soon enable us to denominate some of our foreign borrowings in ECU's. Financially, this would expose us to smaller risks of exchange losses than alternative denominations in national currencies such as the mark or the Swiss franc. Politically, it would be a concrete and spectacular demonstration of our will to support the new European Monetary System, and be far more acceptable than borrowings in any *national* currency other than the dollar, opening us to the accusation, for instance, of making the dollar a satellite of the mark.

Secondly, a reinforced EMCF — and later European Monetary Fund — should facilitate the effective concertation of joint intervention and management of European exchange rates vis-à-vis the dollar. It should also provide an additional mechanism for the "substitution accounts" envisaged above. Reluctant dollar holders could exchange them for ECU's, if they wished, as well as for SDR's.

The *quid pro quo* of the ECU exchange guarantee granted by the U.S. to the EMCF would be a substantial lowering of interest rates on our obligations, and their consolidation into longer term maturities. This consolidation vis-à-vis the EMCF would leave intact the "liquid" character of the ECU claims held on it by the national Central Banks in exchange for their dollars, insofar as intra-EMS balance-of-payments disequilibria could be settled by mere book-keeping transfers of ECU balances from one member country to another. This liquid character would also be preserved for the financing of European deficits toward the United States — and other dollar-area countries — if our obligations toward the EMCF were expressed in the most appropriate form, *i.e.* in the form of "*consols*" without any imperative repayment date. "Consol" bonds paying interest to their holders, but repayable only at the initiative of the debtor — mostly

[13] Agreement on this technique, however, is likely to require a parallel agreement of some sort on the complementary proposal of the IMF Executive Directors and the Committee of Twenty on "asset settlements". See the remarks of M. Szasz, and others, on this topic in *EMS: the Emerging European Monetary System*, published by IRES, Louvain-la-Neuve, Belgium, 1979.

through open market operations — used to be a most traditional and prestigious means of borrowing for the British Government, and — under the name of "rentes perpétuelles" — for the French Government. They could be made similarly familiar and attractive today, especially if coupled with a "contingent" repayment obligation in the event that present balance-of-payments disequilibria were reversed and our creditors were again to incur substantial deficits toward the United States.

It would, moreover, express operationally an obvious and inescapable truth, *i.e.* that "real" repayment of international credits can only be effected through the recovery of a surplus position by the debtor. All that financial arrangements can do, otherwise, is to reshuffle among the creditors the claims on a deficit country, but it is equally true that these creditors can only receive "real" repayment for their claims by running deficits. I feel that the suggestions above would help dispel the financial fog clouding these transactions — and often misleading the transactors themselves into unfortunate and ineffective policy decisions — and adjust international lending practices to the facts of life.

Note also that the "consols" accumulated by the EMCF — or a reformed IMF — should be negotiable in the market, under agreed conditions, whenever advisable to mop up excessive, inflationary, levels of liquidity.

3. *Progress toward Worldwide Reforms*

Some people still view regional monetary cooperation as the antithesis of worldwide monetary cooperation. I took the opposite view when I helped plan and negotiate the *European Payments Union*, which provided in the 1950's a most spectacular demonstration of the *complementarity* of these two approaches. The EPU did much more, indeed, than the IMF in those years to restore convertibility between the participating currencies and the dollar, as well as among themselves.

I am convinced that the success of the EMS experiment toward its basic objectives, and of the indispensable cooperation between the EMS and U.S. authorities, might at long last break the deadlock which has paralyzed, since Jamaica, the previous determination to restore a workable world monetary order. I hope I am not entirely a

"loner" and a dreamer in feeling that floating rates and the Second Amendment to the IMF Articles of Agreement should not relegate to the garbage can all the previous proposals for IMF reform, ironed out over ten years of continuous, intensive negotiations. May I refer those who are open to argument in this respect to my inaugural McCloy lecture of last November published in the Princeton Essays in International Finance under the title *"Gold and the Dollar Crisis: Yesterday and Tomorrow"* (particularly pp. 11 and 12). The revolutionary developments of recent years certainly require a modification of previous proposals for reform, but to enlarge them — particularly to deal with the fantastic explosion of private international credits — rather than to emasculate them.

1) First and foremost, of course, should be the actual implementation of the often reiterated pious wish to substitute a reformed SDR for the dollar as well as for gold in international reserves and settlements. The latest IFS estimates show how far we are from that goal: SDR's and Reserve Positions in the Fund accounted each, last May, for less than 3% of world reserves, as against 44% for gold (valued at market prices) and 51% for foreign exchange holdings. Let us hope that the IMF Belgrade meeting resolution regarding SDR "substitution accounts" will prove a first step on the long road still ahead. The mopping up of outstanding gold and dollar holdings through "substitution accounts", however, would be useless — and difficult to negotiate — if it were not complemented by the radical reforms to which it should be a mere prelude, *i.e.* those that will: (i) limit the *future* expansion of the world reserve system to what is needed to make it an engine of world stability rather than of world inflation; and (ii) attempt to earmark this growth for the financing of high-priority economic and social objectives commonly agreed, rather than for the haphazard financing of U.S or other reserve centers' deficits.

I would plead again, as a way to meet the first of these objectives, for a simple but only *presumptive* rule *à la* Milton Friedman: the IMF should be directed to expand its total lending and investment portfolio at a rate of 4 to 6 per cent a year, consistent with the reserve requirements of non-inflationary growth of world trade and production. Weighted voting of 2/3, 3/4, or even more, should be required to authorize substantial departures from this presumptive target. For it to have the desired effect, moreover, the monetary authorities should invest *all* of their future surpluses in SDR's — rebaptized, of course,

and made more attractive to members — and eschew any purchase of gold and foreign exchange, except for minimum working balances in foreign currencies still needed for interventions in the market until SDR's are made available — as they should be — to commercial banks, and even other holders.[14] Particularly encouraging in this respect are the forward-looking *"Thougts on an International Monetary Fund based fully on the SDR"* of the Economic Counsellor and Director of the Research Department of the International Monetary Fund: J.J. Polak.[15]

As for the second objective, it would flow automatically from the fact that all reserve growth would become the result of agreed Fund decisions. These should include the type of operations financed in the past by the Fund — including those covered by the "General Agreements to Borrow" — but add to them those now made possible by the substitution of SDR's for gold and foreign exchange reserves, and not necessarily limited — as brilliantly explained by Professor Machlup[16] — to short-term lending. An expansion of IMF operations consistent with the first objective above should leave room for such operations. They might take the form of IMF investments in long-term bonds, *or even consols*, issued by various agencies such as the World Bank, its affiliates, other Regional Development Banks, and even by other international agencies such as the World Health Organization, etc.

2) Two further aspects of this reshaping of the international monetary system deserve a few comments. The first is the need to take into consideration the incredible mushrooming of international credit financed by private sectors, particularly through Euro-currency credits and Euro-bond issues. The rough and incomplete estimates reported by the BIS[17] show a *net* increase of about $ 330 billion in these private lending operations over the last three years ($ 535 billion gross), *i.e.* more than 2 ½ times the reported increase of $ 127 billion in the foreign exchange investments of central banks, and 60 times that of SDR allocations and IMF lending.[18] Some distinguished

[14] To the extent that more substantial dollar accumulation were deemed necessary in a transition period, it should be deducted from the authorized Fund lending and investment operations.

[15] Recently published by the Fund as No. 28 in its Pamphlet Series.

[16] Particularly in "The Cloakroom Rule of International Reserves: Reserve Creation and Resources Transfers", *Quarterly Journal of Economics*, August 1965.

[17] In its June 1979 *Annual Report*, p. 104.

[18] See accompanying Table IV. Note, however, that a significant portion of these reported increases, valued in dollars, reflect the impact of the dollar depreciation over these years (from 0.85422 to 0.76758 SDR's per dollar) rather than new lending.

economists — from Academia as well as from the U.S. Treasury — have been arguing on this basis that the reforms previously advocated as necessary to arrest the inflationary explosion of reserve creation have not only been made unnecessary by the generalization of floating rates, but have also become irrelevant anyway in view of the ease with which countries can now finance continuing deficits through their borrowings from the private market, rather than through reserve losses or borrowing from the IMF. I would draw from the same facts the opposite conclusion, *i.e.* that any meaningful attempt to reduce persistent world inflation and balance-of-payments disequilibria must deal with both of their two major sources in recent years:

a) The disordinate financing of reserve-centre borrowings, which floating rates have failed to reduce significantly; and

b) the disordinate growth of private financing, which could not have reached such proportions, anyway, if the U.S. dollar had not acquired unwittingly the privilege — and burden! — of being accepted by central banks as well as by commercial banks and their customers as a "parallel world currency".

TABLE IV

MAIN SOURCES OF INTERNATIONAL LENDING: 1976-78

	In billions of dollars			% shares of 1976-78 increases
	At the end of 1975	At the end of 1978	1976-78 increases	
I. *Creation of Monetary Reserves:*	**178.8**	**311.8**	**133.0**	**29%**
A. Central Banks' foreign exchange claims	160.3	287.7	127.4	27%
B. SDR allocations	10.9	12.1	1.2	—
C. Net IMF credit	7.6	11.9	4.3	1%
II. *Private Market (Net)*			**330.5**	**71%**
A. Commercial Banks' foreign claims	285.0	540.0	255.0	55%
B. Flotation of International Bonds			75.5	16%
III. *Total* (I +II)			**463.5**	**100%**

Sources:
I. *International Financial Statistics* (August 1979), converting SDR estimates into U.S. dollars. Net IMF Credit (line I C) is "Use of Fund Credit" minus undistributed IMF surplus.
II. *Bank for International Settlement, Annual Report* (June 1979), p. 104.

Brief Comments:
The 84% growth of international reserve investments and commercial banks' foreign exchange claims alone (lines I and II A) over the last three years is primarily due to the latter, the foreign lending and investment operations of commercial banks being about double those of central banks, and 46 times those of the IMF.

My second, and final, observation is that the reform path outlined above should — and undoubtedly will — modify fundamentally the distribution of functions and responsibilities between the IMF, the EMF, and other regional monetary groups already in existence and likely to emerge in the future. The financial, economic, and most of all political, scope for monetary cooperation and mutual commitments is obviously much broader among highly interdependent countries — keenly conscious of this interdependence — than that conceivable at this stage on a worldwide scale between more heterogeneous groups of countries less interdependent from one another.

A few figures illustrate the point. Exports to other Community countries account for 52% of total exports for the Community as a whole, ranging from a near-high of 72% for Belgium to a low 38% for the United Kingdom. This is certainly part of the explanation of the greater degree of enthusiasm shown in Belgium than in the United Kingdom for economic and monetary union, particularly if one considers also the greater dependence of GNP on exports for Belgium (50%) than for the United Kingdom (30%). Merchandise exports to the Community account for 33% of Belgium's GDP as against 9% for Britain (see Table V). Yet exports to the Community are for all its members a multiple of their exports to their main outside customer: the United States. They are about 4 times as large for Britain, at the low end of the spectrum, and as much as 17 times for Belgium. The crucial importance of the United States — and of the dollar — in Community policies and institutional arrangements derives primarily from other reasons, such as:

a) the difficulty of changing deeply imbedded psychological attitudes, market habits and bureaucratic routines inherited from the past; and

b) most of all, the still enormous weight of the United States as an economic, political, and military power in the rest of the world, as well as in Europe.

TABLE V

ECONOMIC DEPENDENCE ON INTRA-COMMUNITY EXPORTS (IN 1978)

	in billions of ECU's			in % of exports to the world		
	Community Total	Belgium-Luxembourg	United Kingdom	Community Total	Belgium-Luxembourg	United Kingdom
I. *Exports to Europe:*	**252**	**28.5**	**31.2**	**70**	**81**	**56**
1. to Community countries	186	25.2	21.2	52	72	38
2. to other Western Europe	53	2.7	8.6	14	8	15
3. to Eastern Europe	13	0.7	1.5	4	2	3
II. *Exports to the United States*	**23**	**1.5**	**5.2**	**6**	**4**	**9**
III. *Exports to the Rest of the World*	**84**	**5.1**	**19.6**	**24**	**15**	**35**
IV. *World total*	**360**	**35.1**	**56.1**	**100**	**100**	**100**
1977 % Share in GDP of:						
I. Total exports of goods and services				28	50	30
II. Merchandise exports to the Community				12	33	9

Sources: European Communities: *Eurostat*
(1) For merchandise trade: *Monthly External Trade Bulletin*, Special Number 1958-1978, pp. 21-22; and *EC Trade by Community Classes and Main Countries*, June 1979, pp. 4-5.
(2) For GDP and exports of goods and services: *National Accounts ESA, Aggregates, 1960-1977*, pp. 95, 115 and 123.

Similar observations could be made — and documented — for other areas of the world. A more decentralized structure of monetary cooperation than that of Bretton Woods is long overdue. It would have, to my mind, a triple advantage:

1) to permit a fuller exploitation of the wider potential for realistic cooperation that can be elicited on a regional rather than a world scale.

2) To relieve the IMF of unnecessary responsibilities, and enable it to concentrate its time and attention on those which cannot be discharged as, or more, efficiently on the regional scale.

3) To make wholehearted participation in the IMF more attractive and feasible to disaffected countries, such as many less developed countries, and particularly to make it possible for the

Communist countries, unable to adjust their mutual relations to rules and norms derived from the market — less centrally planned — economies of the capitalistic world, but that would not always make sense for their own economies.

Louvain la Neuve

ROBERT TRIFFIN

ANNEX TABLES

1. Size, Sources, and Distribution and World Monetary Reserves: 1913-1978
2. Size, Sources, and Distribution of Reserve Increases: 1949-1978
3. The U.S. Balance-of-Payments: 1960-1978
4. Regional Pattern of World Exports in 1978.

TABLE 1

SIZE, SOURCES, AND DISTRIBUTION OF WORLD MONETARY RESERVES: 1913-1978

(in billions of dollars or SDR's)

End of	1913	1937	1949	1959	1969	1972	1975	1978
SOURCES								
I. *World gold* in billions of SDR's, at 35 SDR's per ounce throughout	**4.1**	**25.3**	**34.4**	**39.9**	**40.8**	**41.2**	**41.1**	**40.1**
II. *Credit*, in billions of SDR's	**0.7**	**2.4**	**11.1**	**17.0**	**37.9**	**105.3**	**152.7**	**239.3**
A. Foreign exchange	0.7	2.4	11.0	16.1	33.0	95.9	136.9	220.8
B. SDR allocations and IMF credit:	—	—	0.2	0.9	4.8	9.4	15.8	18.5
1. SDR Allocations	—	—	—	—	—	9.3	9	9.3
2. IMF credit	—	—	0.2	0.9	4.8	0.1	5.5	9.2
III. *Impact of Gold-$ Fluctuations*			**–0.3**	**0.1**	**0.2**	**44.2**	**149.6**	**291.5**
A. On gold valuation:			–0.3	0.1	0.2	35.2	123.6	219.0
1. Gold-SDR rate			–0.3	0.1	0.2	29.2	99.6	158.8
2. SDR-$ rate			–	–	–	6.0	24.0	60.2
B. On credit valuation (SDR-$ rate only)			–	–	–	9.0	26.1	72.5
Total reserves, in billions of $	**4.8**	**27.7**	**45.2**	**57.0**	**78.9**	**190.7**	**343.4**	**570.9**
DISTRIBUTION								
Total Reserves, in billions of SDR's	**4.8**	**27.7**	**45.5**	**57.0**	**78.7**	**146.6**	**193.8**	**279.4**
I. United States	1.3	12.8	26.0	21.5	17.0	12.1	13.6	15.0
II. Other countries	3.5	14.9	19.5	35.5	61.7	134.4	180.2	264.4
A. OPEC			1.2	2.5	4.1	10.0	48.3	46.2
B. Other countries			18.3	32.9	57.6	124.4	131.9	218.2
1. Developed			11.0	26.3	45.7	104.7	105.9	165.4
2. Less developed			7.3	6.6	12.0	19.7	26.1	52.8

Notes

1. For 1913 and 1937 estimates, see footnotes to Table 8, pp. 66-67 of my Princeton Study in International Finance (no. 12, June 1964): *The Evolution of the International Monetary System: Historical Reappraisal and Future Perspectives*. Gold holdings in 1913 are valued at $ 20,67 per ounce. Its revaluation to $ 35 per ounce in 1934 accounts for $ 11,4 billion of the $ 25,3 billion 1937 world gold estimate.

2. All other estimates are calculated from the international reserve tables of the annual issue of *International Financial Statistics 1979*. Note that IFS tables show the *composition* of *countries'* reserves, rather than the origin, or *sources* of reserves. They include therefore under "Reserve Positions in the Fund" the impact of gold and SDR transfers by countries to the Fund, attributed here to *world gold* and to total SDR *allocations*. My estimates for IMF credit, as a source of reserves, include only the "Use of Fund Credit" *plus* IMF gold deposits and investments in U.S. Government obligations (only from March 1956 through January 1972) and *minus* a slight discrepancy (rising to about $ 1 billion in 1972-78) arising mostly from the Fund's undistributed surplus.

Slight discrepancies in the IFS total for reserve distribution in 1949 and 1959 have been ascribed to the "Less Developed" Group of countries.

TABLE 2

SIZE, SOURCES, AND DISTRIBUTION OF RESERVE INCREASES: 1949-1978

	From Adam and Eve through	10 Year increases		3 Year increases			9 year increases	6 year increases
	1949	1949-59	1959-69	1969-72	1972-75	1975-78	1969-78	1972-78
SIZE								
1. in billions of $	45	12	22	112	153	227	492	380
2. in billions of SDR's	46	11	22	68	47	86	201	133
RATES OF GROWTH over period								
1. of $ estimates		26	35	142	80	66	623	199
2. of SDR estimates		25	38	86	32	44	255	91
Annual growth rates								
1. of $ estimates		2	3	34	22	18	25	20
2. of SDR estimates		2	3	23	10	13	15	11
SOURCES (for $ estimates)								
In billions								
I. *Gold*	**34**	**6**	**1**	—	—	—	—	**—1**
II. *Credit*	**11**	**6**	**21**	**67**	**47**	**87**	**201**	**134**
A. Foreign exchange	11	5	17	63	41	84	188	125
B. SDR allocations & IMF credit	—	1	4	5	6	2	14	9
III. *Impact of gold-$ fluctuations:*	—	—	—	**44**	**105**	**142**	**291**	**247**
A. gold-SDR rate	—	—	—	29	70	59	159	130
B. SDR-$ rate	—	—	—	15	35	83	133	118
In % of total:								
I. *Gold*	**76**	**47**	**4**	—	—	—	—	—
II. *Credit*	**24**	**50**	**95**	**60**	**31**	**38**	**41**	**35**
A. Foreign exchange	24	43	77	56	27	37	38	33
B. SDR allocation & IMF credit	1	6	18	4	4	1	3	2
III. *Impact of gold-$ fluctuations:*	**—1**	**3**	**—**	**39**	**69**	**62**	**59**	**65**
A. gold-SDR rate	—1	3	—	26	46	26	32	34
B. SDR-$ rate	—	—	—	13	23	36	27	31
DISTRIBUTION (for SDR estimates)								
In billions:								
I. United States	**26.0**	**—4.5**	**—4.5**	**—4.9**	**1.5**	**1.4**	**—2.0**	**2.9**
II. Other countries:	**19.5**	**16.0**	**26.2**	**72,7**	**45.8**	**84.2**	**202.7**	**130.0**
A. OPEC	1.2	1.3	1.5	5.9	38.3	—2.1	42.1	36.2
B. Other countries:	18.3	14.6	24.7	66.8	7.5	86.3	160.6	93.8
1. Developed	11.0	15.3	19.4	59.0	1.2	59.5	119.7	60.7
2. Less developed	7.3	—0.7	5.4	7.7	6.4	26.7	40.8	33.1
In % of world total								
I. United States:	**57**	**—39**	**—21**	**—7**	**3**	**2**	**—1**	**2**
II. Other countries:	**43**	**139**	**121**	**107**	**97**	**98**	**101**	**98**
A. OPEC	3	11	7	9	81	–2	21	27
B. Other countries	40	127	114	98	16	101	80	71
1. Developed	24	133	89	87	3	70	60	46
2. Less developed	16	–6	25	11	14	31	20	25

Sources and notes: see table 1

TABLE 3

THE U.S. BALANCE OF PAYMENTS: 1960-1978
(in billions of dollars)

	Total 1960-78	Yearly Averages 1960-69	1970-72	1973-78	Year 1978	% Share in Total Financing 1960-69	1973-78
I. *Recorded Debt Increase (-)* of	—320	—5	—18	—36	—64	113	91
A. *Treasury and Banks* to:	**—243**	**—3**	**—13**	**—29**	**—53**	**69**	**73**
1. Official Institutions	—166	—1	—16	—19	—34	18	46
2. Other (mostly Banks)	—78	—2	3	—11	—19	50	27
B. *Other*	—77	*—2*	*—5*	*—7*	*—11*	44	18
II. *Statistical Discrepancy*	*—5*	*1*	*4*	*—4*	*—11*	*—13*	*9*
III. TOTAL (I & II), *financing:*	**—325**	**—4**	**—14**	**—40**	**—75**	**100**	**100**
A. *Current U.S. Deficit (-)* (no sign = surplus)	**76**	**5**	**—**	**4**	**—11**	**—121**	**—10**
1. Net Earnings on Past Investments	167	5	7	16	22	—114	—40
2. Other	—91	—	—7	—12	—32	—6	30
B. *Capital Exports* (-):	**—401**	**—9**	**—14**	**—44**	**—64**	**222**	**110**
("Recycling")	5	—	2	—1	1	—11	2
1. Monetary Reserves	—120	—1	—2	—17	—33	18	43
2. Bank Claims	—83	—3	—4	—6	—8	81	16
3. Foreign Aid	—203	—6	—10	—20	—24	133	49
4. Other							

TABLE 3A

	1972	1978	Dec. 1978
End of Period Average Depreciation (-) or Appreciation of the $, in %, since May 1970, vis-à-vis:			
1. Twenty Major Currencies	–10	–21	–24
2. Swiss Franc	–13	–59	–62
3. German Mark	–13	–45	–49
4. Japanese Yen	–16	–42	–45
5. Pound Sterling	–4	+25	+21

Sources:
Survey of Current Business and *International Financial Statistics.*

TABLE 4

REGIONAL PATTERN OF WORLD EXPORTS IN 1978
(in % of exports to the world)

EXPORTS TO → / FROM ↓	I Eur. Or. Areas	II Western Hemisph.	III Asia (1)	IA. WESTERN EUROPE Total	European Community	Other W. Europ.	OTHER EUROPE ORIENTED AREAS Midd. East & Afr. (1)	Communist Countries	Australia N. Zeal. S. Africa	II. WESTERN HEMISPHERE USA	Other	III. ASIA (1) Japan	Other
I. *Europe-Oriented Areas*	**75**	**14**	**9**	**59**	**45**	**14**	**11**	**4**	**2**	**9**	**5**	**5**	**4**
A. *Western Europe*	*85*	*10*	*4*	*66*	*50*	*15*	*13*	*5*	*2*	*6*	*3*	*1*	*3*
Europ. Community	85	10	4	66	51	15	13	*4*	2	6	3	1	3
Other Western Europe	86	10	4	62	45	16	12	12	1	6	3	2	2
B. *Middle East. & Africa*	*48*	*30*	*21*	*41*	*33*	*8*	*5*	*1*	*1*	*19*	*11*	*14*	*7*
Oil-Exp. Countries	43	33	24	38	31	8	3	—	1	21	13	16	8
Other Middle East	70	10	13	38	30	9	20	10	2	9	1	6	7
Other Africa (2)	74	18	7	57	49	8	12	4	1	12	6	4	3
C. *Communist Countries* (3)	77	*6*	*17*	*65*	*35*	*30*	*11*	(*)	*1*	*3*	3	*9*	*9*
D. *Australia N. Zealand S. Africa*	*40*	*16*	*31*	*26*	*22*	*4*	*6*	*4*	*4*	*13*	*3*	*19*	*12*
II. *Western Hemisphere*	**41**	**44**	**14**	**25**	**20**	**5**	**11**	**3**	**2**	**20**	**23**	**7**	**6**
A. United States	49	32	18	28	22	6	15	3	3	X	32	9	9
B. Canada	18	70	8	10	9	1	4	3	1	68	3	6	2
C. Latin America	42	50	6	31	24	7	6	5	—	33	16	5	2
III. *Other Asia*	**41**	**31**	**27**	**18**	**14**	**4**	**15**	**5**	**4**	**25**	**6**	**7**	**20**
A. Japan	43	33	22	16	11	4	17	7	3	26	7	X	22
B. Other countries	38	28	34	21	17	3	12	3	2	25	3	16	18
IV. *World*	**64**	**22**	**13**	**46**	**36**	**11**	**11**	**4**	**2**	**14**	**9**	**6**	**7**

Source: Direction of Trade Yearbook 1979 (International Monetary Fund)

NOTES:
(1) Other than oil-exporting countries.
(2) Other than South Africa.
(3) Incomplete estimates excluding most of intra-trade. See *Source* for other explanations and qualifications. Exports to unspecified areas (slight, except for "Other Middle East" and "Australia, New Zealand and South Africa") account for differences between *horizontal* totals and 100%.

BRIEF COMMENTS:
1. Intra-trade is much larger for Western Europe, and even the European Community alone, than for other geographical areas. It is also very significant within the Western Hemisphere, especially between Canada and the United States.
2. The share of Western Europe in the export trade of the "Oil-exporting countries" and of "Australia, New Zealand and South Africa" would not orient these areas as decisively as the others toward a European Area. Yet, their main ties would be in that direction rather than toward either the Western Hemisphere or Asia, especially if account is taken of their geographical location and import trade for the first group; and of their financial and political links with Britain for the latter.