

## Altman on Triffin

### A Rebuttal\*

May I first confess to my embarrassment at having to comment on Mr. Altman's excellent paper? It is in the nature of a rebuttal to concentrate on points of disagreement, and this is particularly unpleasant in the present case. I have learned a lot from Mr. Altman's paper and from his previous writings on this topic. I cannot, moreover, but feel inordinately flattered at having my views so thoroughly dissected and scrutinized by this able advisor of the International Monetary Fund. Yet, I feel equally disappointed at the uniformly negative tone of his criticisms, and at the absence of any positive and constructive alternatives to the proposals which I have ventured. I would have welcomed a more candid recognition of the problems which we face, and an effort to amend, rather than merely dismiss, my own suggestions for dealing with them. Such amendments are certainly necessary. It would be a miracle indeed if any plan of a lone student, isolated in the ivory tower of his University, proved fully acceptable to the practical experts and responsible statesmen of several scores of independent nations. Even in my moments of wildest optimism, I have never hoped to be able to do more than to initiate and stimulate a broad discussion of the long overdue reforms obviously necessary to adjust to modern needs and conditions an international monetary system inherited from a long series of uncorrelated — and often haphazard — reactions to the crises of yesteryears. The international negotiations that will soon become indispensable to that end would benefit far more

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from constructive criticism and alternative suggestions than from complacency with what now exists, but obviously cannot endure.

### I. A Wrong Diagnosis?

My diagnosis of the present problem can be expressed in a nutshell:

1. The present sources of increase in world reserves impart a most dangerous vulnerability to the international monetary system, and to the key currencies upon which it is becoming increasingly dependent. Monetary reserves outside the United States and the United Kingdom are built on a decreasing proportion of gold and an increasing proportion of foreign assets, mostly sterling and dollars. The latter proportion rose from 9 per cent in 1913 to 36 per cent in 1928, but collapsed to 13 per cent in 1933 with the first breakdown of the gold-exchange or key currencies standard (1). It has now risen to well over 50 per cent of world reserves, but undermined gravely the position of one of the key currencies — sterling — in the early postwar years, and that of the other — the dollar — today. A repetition of the 1931 breakdown of the gold exchange standard may yet be avoided, but it has become a distinct possibility, widely discussed in the financial press all over the world.

2. Even if the United States were to regain tomorrow "overall" equilibrium in its balance of payments, it would remain saddled with an enormous burden of floating foreign debt — \$19.3 billion as of the end of August 1960, nearly triple the size of our so-called "free" gold reserves — which would handicap severely its freedom of monetary management during the course of any future recession

(1) May I take objection, in passing, to Mr. Altman's suggestion that I might regard the extension of the gold exchange standard in the 1920's as having possibly been "a primary factor in the deflation that began in 1929". All I said is that it "led... to the devaluation of the pound sterling, to the collapse of the international gold exchange standard, and to the consequent *aggravation* of the world depression" (*Gold and the Dollar Crisis*, p. 9). That is enough, to my mind, to condemn the system without blaming it in addition for other cyclical developments, the world agricultural crisis, and other sins of commission or omission in the economic policies of the 1920's.

I shall, in this paper, refrain from further comments of this sort on minor disagreements upon points of detail, irrelevant to the main issues under consideration.

in domestic employment and economic activity. Our "overall" balance of payments is usually measured by the sum of our current gold losses and increases in foreign dollar balances. Large conversions of dollar balances into gold might leave us in "overall" equilibrium — our gold losses being offset by the parallel reduction in our indebtedness abroad — and yet lead to a major dollar crisis forcing us to choose between deflation, devaluation, an embargo on gold, drastic cuts in our foreign aid or military defense programs, tariff increases, other trade or exchange restrictions, etc., or various possible combinations of such unhappy "policies".

3. Disregarding such catastrophic — but, let us hope, improbable — possibilities, the fact remains that the restoration of overall equilibrium in the United States balance of payments would dry up the major source by far of current liquidity and monetary reserve increases for the world. The rapid and persistent increase of official dollar balances over the last decade accounts for more than 50 per cent of the rise in world's reserves during that period. Together with U.S. gold losses, it made up two thirds of foreign countries' reserve increases over the ten years 1950-59, and more than 90 per cent over the two years 1958 and 1959.

I cannot discover in Mr. Altman's criticism of my diagnosis any strong rebuttal, or even comprehensive appraisal, of my first two points. They are largely ignored or swept under the carpet. As for the third, it is unconvincing to him, primarily because he considers as "at best... unproven", and "at worst... incorrect" my "findings of serious reserve deficiency..., at least for the next five or ten years. It may be argued that ten years is not a long time, and that the world should now anticipate developments over a much longer period. As to this, opinions differ" (paragraph 66, page 33).

Mr. Altman's detailed arguments on this point are spread throughout his paper. They boil down to the fact that "Triffin's view of the required growth of reserves is essentially a mechanistic one. It is simply not true that the need for monetary reserves can be read off arithmetically from a table relating reserves to trade" (paragraph 38, page 17). The quality and distribution of reserve assets should be taken into account, as well as each country's reserve policies. Net reserves may be as important as gross reserves. Past

forecasts of reserve deficiency have often proved to have been wrong, etc.

I don't disagree with any of these points, but — as Mr. Kennedy said to Mr. Nixon — I don't recognize myself in the straw man that Mr. Altman wishes to knock down. I prefaced my whole discussion of reserve measurements and adequacy criteria in *Gold and the Dollar Crisis* (see particularly, pp. 35-37) with very much the same arguments as Mr. Altman. I also explicitly "confessed" there that my reason for retaining "the ratio of gross reserves to annual imports... as a first, and admittedly rough, approach to the problem of reserve adequacy" was the fact that this approach had been followed — with similar qualifications — by the famous IMF staff study of 1958 on *International Reserves and Liquidity*, whose main author — or so at least rumor has it — is precisely... Mr. Altman. I also warned the reader that the "results would admittedly be too crude to determine any precise level of reserve adequacy, but they will prove more than sufficient to indicate whether current or prospective reserve levels are likely to facilitate, or seriously hamper, the smooth functioning of international currency convertibility" (p. 36).

I followed exactly, in the chapter appraising prospective reserve adequacy over the next ten years (Chapter 5, pp. 47-58), the very procedure adopted in the Fund's study. I questioned, however, the wisdom of excluding from their calculations any reserve increase for the high reserve countries without allowing, on the other hand, for any reconstitution of reserves by at the least some of the major low reserve countries which had given evidence of having such policies in mind. I questioned also the wisdom of accepting as a basis for the IMF optimistic forecasts of reserve adequacy a future growth rate based on past averages of "normal" peacetime experience diluted "with the abnormally low, and in fact predominantly negative, growth rates of wartime years and of the 1930's world depression. An expected adequacy of reserves based upon the assumption of a third world war or of another deep and protracted world depression is hardly encouraging as a guide to policy" (*Gold and the Dollar Crisis*, p. 48).

I am as surprised to find no answer to these two questions I raised against the IMF calculations, as I am to be profusely criticized for having followed them too slavishly in order to develop and appraise their own implications.

Let me, therefore, clarify — if need be — my own position about reserve adequacy. I do not now claim, and have never claimed, that "the level of reserves in 1957 or in 1958, the years used by Triffin as bases for reserve calculations, represented the minimum reserves required by the noncommunist world, and that in the future these reserves must grow as fast as world trade" (Altman, paragraph 38, p. 17). What I said is that "there can be little doubt that the 35 per cent *average* level reached in 1957 by all countries outside the United States and the United Kingdom was on the low side of any reasonable estimate of world liquidity requirements, and that any further contraction below that level would make it very difficult for a number of key countries to adhere firmly to the convertibility policies which they would otherwise be willing and eager to pursue" (*Gold and the Dollar Crisis*, p. 46).

Mr. Altman points to the satisfactory increase of world gold and foreign exchange reserves since 1956 as contradicting my forecast that *gold alone* would not suffice to satisfy the expected growth of post-1957 reserve requirements in an expanding world economy. What his own figures (on p. 28 of his paper) indicate, however, is that the expansion in the world's stock of monetary gold over this period — \$2.1 billion — played only a minor part in the very rapid, and indeed more than adequate, expansion of monetary reserves outside the United States. These increased by more than 12 per cent over this period in spite of exceptionally large disbursements to the IMF — in repayment of past loans and as subscriptions to the Fund's capital increase — of substantial sales of foreign exchange to commercial banks, and of the exclusion from reserve calculations at the end of this period of the considerable claims previously held on EPU — \$1.3 billion — and included in the reserve figures for 1956. Reserves outside the United States progressed indeed at a highly satisfactory rate over this period, but this had far less to do with gold production than with the enormous drain on the United States net reserve position. United States gold losses and increasing short-term indebtedness abroad contributed more than \$3.6 billion to the reserve increases of foreign countries, even though at a very uneven pace: *minus* \$0.9 billion in 1957, *plus* \$3.0 billion in 1958 and *plus* \$1.6 billion in 1959.

This brings out, indeed, the major flaw in Mr. Altman's criticism of my discussion of prospective reserve adequacy. He takes

me to task for what he does himself, i.e. for ignoring the structure and distribution of world reserves when discussing their overall level. My own discussion, however, was essentially directed at stressing the inadequacy of *gold* production alone as a source of reserve increases. I never denied that reserves could be kept at an adequate level as long as the United States could afford an overall deficit of \$3 billion to \$4 billion a year in its balance of payments — as has been the case ever since the end of 1957 — and as long as foreign countries continued to accept dollar IOU's in lieu of gold, in settlement of a large portion of these deficits. Quite obviously, however, it would be foolhardy to regard such assumptions

SOURCES OF INCREASES IN WORLD RESERVES, 1914-1959

	Total Increase (1)	From Western Gold Sources (2)	From Other Sources				
			Total	Coin Withdrawal	Dollar Devaluation	USSR Gold Sales	Foreign Exchange
A. In billion of dollars							
1914-1928	8.5	3.2	5.3	2.5	—	(4)	2.8
1929-1933	7.2	0.9	6.4	0.8	7.9 (3)	(4)	- 2.3
1934-1938	7.5	6.8	0.7	—	—	- 0.1	0.8
1939-1949	19.1	8.7	10.4	—	—	0.3	10.1
1949-1959	12.8	4.1	8.2	—	—	1.1	7.5
1914-1959	55.1	23.7	31.4	3.3	7.9	1.3	18.9
B. In % of Total							
1914-1928	100	38	62	30	—	(4)	32
1929-1933	100	12	88	10	109 (3)	(4)	- 31
1934-1938	100	90	10	—	—	- 1	11
1939-1949	100	46	54	—	—	1	53
1949-1959	100	33	67	—	—	9	59
1914-1959	100	43	57	6	14	1	34

(1) Excluding Soviet bloc countries throughout, as well as IMF currency holdings.

(2) Current gold production in the West, *minus* net sales to, or *plus* net purchases from, private channels. Large net repurchases from private channels (estimated at \$1.7 billion in 1934-37) followed the sterling and dollar devaluations, in sharp contrast to the usual net absorption of gold into hoarding and private uses.

(3) Calculated on the basis of the official parity change of February 1934, following the suspension of gold payments and the *de facto* dollar depreciation in 1933.

(4) Included, until the end of 1933, with Western gold sources.

Sources: These must be regarded as only rough estimates — particularly in the early years of the Table — put together from various IMF and Federal Reserve publications.

as providing a safe and viable basis upon which to meet indefinitely future increases in world reserves. Mr. Altman seems to think that it definitely is, "at least for the next five or ten years" (paragraph 66, on page 33). On this too — to borrow from his next sentence — I trust that "opinions differ".

Let me finally note, to close this discussion, that the problem is not a new one, but a very old one. Gold has long ceased to feed more than a fraction of annual increases in world monetary reserves. It contributed less than 40 per cent of such increases over the period 1914-1928, against more than 60 per cent derived from the withdrawal of gold coin from circulation and from the rapid rise in dollar, and particularly sterling, reserves at that time. The revaluation of gold provided more than 100 per cent of the reserve increases of the years 1929-1933, measured in terms of the U.S. dollar, but the collapse of the gold exchange standard *extinguished* at the same time most of the dollar and sterling reserves, which were precipitously converted into gold by their holders. The unprecedented growth of sterling balances accounted once more for the largest part of reserve increases during the second world war, but at the cost of sterling inconvertibility and devaluation. In the last ten years, gold production in the West has contributed little more than a third of reserve increases, more than half of which has been derived from the continued growth of dollar balances, and a smaller, but increasing portion — close to 40 per cent in the last three years — from Russian sales of gold in the Western markets.

My own proposals for dealing with the problem may be open to serious objections, but can somebody seriously defend as preferable the present system under which annual supplies of reserves are utterly dependent upon:

1. the hazards of gold-digging in a country whose economic life may be brought to a standstill tomorrow by the threatening eruption of racial warfare;

2. Mr. Khrushchev's policies about USSR gold sales in the West;

3. the perpetuation of our balance of payments deficits, and the continued acceptance of dollar IOU's by other countries.

Let me turn now to Mr. Altman's objections to my own proposals for a reform of the IMF statutes.

## II. A Controversial Prescription?

My recommendations for a radical reform of the world's monetary system are bound to be "controversial". I fully agree here with Mr. Altman, and hope indeed to benefit from the controversy which he has so brilliantly opened up and which he and others — I also hope — will pursue, enrich, and enlighten, in preparation for a forthcoming renegotiation of the IMF Articles of Agreement.

The first objection of Mr. Altman has already been dealt with above. He sometimes ascribes to me — or thinks my readers will ascribe to me — a typical Chicago School proposal for a "mechanistic" increase of world reserves at an invariable and "almost self-evident" rate of 3 per cent a year. He rightly criticizes such a concept, and recognizes elsewhere that I have never propounded it. Indeed he deplores my unwillingness "to provide it [the IMF] with a statement of policy objective, let alone any specific guides to operations policy" (paragraph 46, on p. 23). This does not prevent him, however, from harping again and again on the "mechanistic" character of my proposals and from concluding that "an expanded IMF with responsibilities toward adequate levels of international liquidity implied by Triffin would be put in the position of attempting to do internationally what no central bank has been willing to attempt nationally" (paragraph 52, on p. 26).

Certainly, no central bank has yet accepted the proposal of Professor Friedman to ensure a constant increase of money supply at a 3 or 4 per cent annual rate, come hell or high water! But the efforts of all central banks have been bent for at least half a century upon the task of facilitating the adjustment of money supply to the attainment of feasible, but non-inflationary, levels of employment and economic growth. They have never hesitated to use so-called sterilization, neutralization or compensatory policies to insulate their economy from unwanted shocks that would interfere with the achievement of this broad objective. They certainly would never have, willingly, abandoned the effective regulation of money supply to chance events comparable to those mentioned above (on p. 37) and on which the provision of international monetary reserves is now utterly dependent. This being said, I agree with Mr. Altman that the task of the expanded IMF can not be laid down in advance in any automatic or mechanistic formula, and that the Fund's authorities will have to "consider a combination of criteria" and

use at all times flexible and intelligent judgment in facing the unpredictable problems of tomorrow.

Secondly, Mr. Altman fears that my proposals might interfere with the rude but beneficial discipline of gold flows (paragraph 28, on p. 13) but he also objects a few pages later (paragraph 33, on p. 16) to the fact that "expansion of the IMF along the lines recommended by Triffin would not by itself eliminate the risks of pressure on the dollar and gold outflows from the United States".

I confess to some embarrassment at having to answer both points at the same time. In brief, my proposals would not weaken the discipline of gold flows, but on the contrary reduce the distortion of their timing which results from the present operation of the gold-exchange standard, as opposed to the gold standard. It is a fact that the piling up of so-called key currency balances under that system postpones the gold flows that would otherwise accompany overall payments deficits. They facilitate — or even stimulate — thereby the continuation of such deficits, but at the cost of weakening the net reserve structure of the key currency countries and exposing them to sudden and large withdrawals of funds at a later date. In spite of its enormous gold reserves, the United States itself would hardly have been able to accumulate overall deficits of more than \$15 billion over the ten years 1950-1959, if the "discipline of gold outflows" had not been considerably relaxed by the acceptance of more than \$11 billion of this amount by foreigners in the form of dollar balances, of which more than \$6 billion in official monetary reserves. Conversely, the fate of our dollar would not be endangered today by the existence of more than \$19 billion of short-term debts abroad, legally convertible into gold, either directly or indirectly.

By outlawing the accumulation of *national* currencies as *international* reserves, my proposals would tend to restore, at least in part, the normal discipline of gold flows. They would not, however, eliminate automatically the weakening and distortion of that discipline resulting from the flows of *private* short term funds. This would remain a problem to be dealt with by the monetary authorities of each country, but which the new IMF would nevertheless be in a much stronger position to help them solve, through its own loan and investment policies.

Mr. Altman cites some disadvantages which the new system might have for the key currency countries, i.e. for the United States

and the United Kingdom. They might, for instance, be called upon to make some amortization payments on the dollar and sterling balances transferred to the new Fund by their present owners, even though — according to my proposals — only as and when this proves useful to the implementation of the Fund's tasks and policies, and only at a maximum pace of 5 per cent a year. Can this be rated as a disadvantage, however, as compared with a situation under which the present owners are free to convert into gold, at any time, the *totality* of these balances? Mr. Altman quotes, in this connection, my expectation that the Fund might well, in the initial years of the new system, seek further dollar and sterling investments of its enlarged resources, thus helping "smooth out the transition from the present system where international liquidity has come to depend increasingly on a continuous increase of such balances". He dismisses this suggestion airily, but mysteriously, with the remark that "it is a fair comment that only an extraordinary reader will share this expectation" (paragraph 49, footnote 2, on p. 25).

Mr. Altman also objects to the exchange guarantee that would automatically be attached, under the Fund's statutes, to the deposits of its members and to its dollar and sterling investments. Yet, this has long been an accepted procedure in all Fund's transactions, including by the way the \$800 million invested by it in U.S. Treasury Bills and funds awaiting investment and for which the same quantity of gold can be re-acquired from our Treasury upon termination of the investment. It was also an accepted procedure in EPU, and seems indeed far more reasonable than a system under which the value of such claims can arbitrarily be written down by any devaluation decision of the debtor.

Mr. Altman also considers (paragraph 29, on p. 14) that my plan would spell the end of the sterling area. Such an interpretation has never been given to my proposals by the British themselves (2) and I think — quoting Mr. Altman out of context — that "it is a fair comment that only an extraordinary reader will share this expectation". After all, I devoted 24 pages of my book (pp. 121-144) to argue that "the management of a world-wide clearing system, and particularly the investment of the large funds derived from its operation, will present enormous administrative and political

(2) See, for instance, the comments of Professor Brian Tew in *International Monetary Cooperation, 1945-60* (Fifth edition, London, 1960), p. 183.

hurdles, which can best be surmounted through some decentralization of the Fund's decision-making process" (p. 128), and went on to describe as examples of such desirable decentralization the setting up of a European Clearing Union and of a European Community Reserve Fund. The suggestions developed in these pages could be similarly applicable to other regional organizations, including Sterling Area arrangements, as long as these do not involve any weakening of the broader, world-wide convertibility and co-operation commitments of their members, but aim on the contrary at consolidating them through additional measures of integration and harmonization reducing the danger of conflicting and mutually defeating national policies.

A more valid objection of Mr. Altman relates to the composition of the Fund's assets. The expansion of the Fund's loans and investments should normally be expected to direct capital mostly to the underdeveloped countries, and I suggested indeed such a general line of policy in my book. Aware, however, that direct lending of this character would be anathema to the more conservative minds among central bankers, I suggested that relatively long term investments for economic development be financed only indirectly "through purchases of IBRD bonds or other securities of a similar character" (*Gold and the Dollar Crisis*, p. 118). The increasing investments in IBRD bonds taken up in recent years by one of the most orthodox of central banks — the Bundesbank of Germany — should help make such a "radical" idea more "respectable" than it would have been otherwise.

More may prove necessary, however, to meet Mr. Altman's objection and get around the "taboos" still prevalent in some circles about the nature of the assets which it is proper for monetary institutions to acquire. Fund's investments could, for instance, be channelled to a greater extent toward older financial centers such as Frankfurt, Amsterdam, Paris, etc. and — notwithstanding Mr. Altman's remark quoted above (see p. 9) — London and New York. This would strengthen these centers' capacity and willingness to finance themselves overseas development. Technically, it would also, it is true, expose them to the accusation that they are making themselves illiquid by "lending long and borrowing short". Yet, this is precisely what they have traditionally done in the past. Moreover, their resulting indebtedness to the Fund would make them far less vulnerable than is now the case to sudden, speculative withdrawals

of the funds invested in their market. The vast resources derived by the Fund from its members' minimum deposit requirements could only grow in time, with the growth of members' reserves, and there would be no reason or occasion impelling the Fund to liquidate suddenly and massively its own investments in members' markets.

Foolproof reassurances in this regard would presuppose, however, the full implementation of my proposals for minimum reserve requirements, including in case of need future increases in such requirements to the extent necessary to preserve the full convertibility of members' deposits into any and all currencies needed by them for international settlement purposes. Mr. Altman stresses the objections which might be raised against such proposals, but fails to point out that the new commitments required of members in this respect would replace — rather be additional to — their present subscriptions to the Fund's capital and their prospective subscriptions to future capital increases. I pointed out, in my testimony before the Joint Economic Committee (see p. 13 of *Gold and the Dollar Crisis*) that such a substitution would result, in the case of the United States, in an *increase* of our gross monetary reserves as well as in the solidation of a large portion of the foreign floating debt which might at any time be cashed for gold at the Treasury.

Last, but not least, Mr. Altman seems to confuse "convertibility" with "convertibility into gold" (see paragraph 12, on p. 6, paragraph 25 on p. 11, and particularly paragraph 50, on p. 26). Fund deposits could always be used at any time — at least in conjunction with members' gold reserves — to make payments anywhere in the world. The fact that minimum deposits have to be kept with the Fund and cannot be withdrawn in gold metal does not make them inconvertible in the most meaningful sense usually attached to that word. The status of such deposits could be compared to that of the legal reserves which must be kept by our banks with the Federal Reserve System and which they cannot liquidate in cash or currency without contravening their minimum deposit obligation. Would Mr. Altman call "inconvertible" sterling balances which can freely be drawn upon to make payments in any and all convertible currencies — including dollars — simply because they cannot be cashed for gold metal at the Bank of England? He is, of course, free to do so, but he and his Fund colleagues should then stop talking about the enormous progress achieved by many countries in 1958 in restoring the "convertibility" of their currency.

### III. Mr. Altman's Alternative Suggestions

In spite of his basic disagreements with my "diagnosis" of the present and prospective international monetary problem, Mr. Altman concedes that something may have to be done to "facilitate further expansion and stability of the structure of international reserves" (paragraph 67, on p. 33). He offers little or no guidance as to what this should be, however, and implies that the present "IMF with its enlarged resources and its proven type of operations" will be equal to the task, although he concedes, in another passage (paragraph 17, footnote 1, on p. 17), that "it may be prudent, as E. M. Bernstein has suggested, to arrange for borrowing in advance of need, by issuing to a small number of countries debentures which could be called for payment to meet large emergencies".

My main reasons for considering these proposals as woefully inadequate to meet the problems of tomorrow should by now be obvious to the reader, and have been discussed at length in the previous writings listed by Mr. Altman. I shall, therefore, limit myself here to a few points of a more technical character, related to some basic defects in the IMF statutes and methods and operations (3).

Article V of the Fund Agreement requires prospective borrowers from the Fund to indicate the particular currency which they wish to purchase and to "represent" that that currency "is presently needed for making *in that currency* payments which are consistent with the provisions of this Agreement". This is, of course, utter nonsense. Such a clause would have meaning only in a world of bilateralism. Under convertibility conditions, the normal way in which a country keeps its currency convertible is by repurchasing from the market, with *any* other widely traded currency that it wishes, excess supplies of its own currency that tend to depress its exchange rate. It can never "represent" to the Fund that it needs to borrow a specific currency — and no other — for that purpose.

In fact, members' requests have so far centered practically exclusively on the U.S. dollar. Over a period during which the United

(3) For a comprehensive discussion and appraisal of the IMF mechanism and operations, and of the reforms needed to make it an effective instrument of international monetary stabilization, see my *Europe and the Money Muddle* (Yale University Press, 1957), Chapter 3, pp. 109-138 and 294-301.

States was the major reserve loser in the world, dollar drawings far exceeded — whether on a net or on a gross basis — 90 per cent of total drawing from the Fund, and aggravated our gold losses and the build-up of our short-term indebtedness to foreign countries. Continental Europe's monetary reserves more than tripled over the same period, but the only continental European currency disbursed by the Fund — on a net basis — was the German mark, for the paltry amount of \$ 100 million.

This absurdity was openly denounced at the last Fund meeting by no less an authority than the British Chancellor of the Exchequer. His words are worth quoting in full:

"There is one further question which I should like to raise. It concerns the method of operation of the Fund. Is there a danger of these operations exacerbating the problem of imbalance because of the tendency for members in short-term difficulties to take drawings from the Fund in only a limited range of currencies? Let me explain my point in a little more detail.

The history of past drawings from the Fund shows that these have been concentrated to a very large extent on the U.S. dollar. This is not surprising. Other member countries naturally wish to draw currencies which they can hold as reserves or can use in exchange operations to maintain their rates. But in our view drawings should, so far as possible, be of the currencies of those countries which are in over-all surplus. Undue concentration on the reserve currencies might have unfortunate consequences in the future. For member countries might wish to draw reserve currencies at a time when those currencies were under strain.

I am sure that this subject is not new to the Fund, but I think it would bear further study now when we can look at it not as something imminent, but as something which could become real at some future date and which in common prudence we ought to provide for. We should be glad to cooperate in such a study and should be ready to make some practical suggestions".

My proposals would meet this problem in the simplest and most automatic manner conceivable, avoiding any need for *ad hoc* discussions and decisions on individual drawings. All Fund loans would be credited to the borrower's deposit account with the Fund, rather than immediately disbursed in any particular currency. Subsequent currency withdrawals by the borrower would be debited from his account and credited to the account of the country whose

currency is drawn, but would not necessarily affect the latter's lending to the Fund. If it is not at that time in net overall surplus in its balance of payments with the world at large, its total reserves — gold and deposits with the Fund taken together — would not increase, and it would be free to cash for gold, if it wishes, any deposits accruing to its account beyond its minimum deposit requirements. Only the countries with overall surpluses and reserve increases would be under obligation to increase their loans to the Fund, thus increasing the Fund's own lending capacity in the currencies which are actually in *final* demand for world settlements.

This points to a major, and broader, difference between the present and the reformed IMF. The present lending capacity of the Fund depends essentially on capital subscriptions, rigidly — and largely arbitrarily — determined by negotiation, and which can be changed only infrequently through new and complex negotiations among members. Three fourths of these capital subscriptions, moreover, are in local currencies — including millions or billions of pesos, rupees, rupiahs, hwans, afghanis, bolivianos, cruzeiros, kyats, etc. — most of which are of no earthly use to the Fund. Others — like the dollar today — may, on the contrary, be used improperly, as pointed out above, at times of heavy dollar deficits. The Fund's resources in the currencies of overall surplus countries may, on the other hand, prove far short of the contributions which Fund lending in these currencies *should* — but does not now — make to the settlement of these countries' surpluses. Finally, while net creditor positions with the Fund do indeed enlarge those creditors' rights to draw upon the Fund, they are expressed in a form which many countries — and particularly the United States — regard as insufficiently liquid to justify their being treated as part and parcel of their monetary reserves. This may reflect the excessive caution prevalent among central bankers, but it is a fact of life. So is the reluctance — deplored by Messrs. Altman and Bernstein — of some of them, including the United States, to draw upon the Fund in cases where such drawings would be eminently justified, but might appear as a sign of weakness, and stimulate undesirable speculation in the gold and exchange markets of the world.

Under my proposals, the rigid quota system would be dispensed with entirely. The Fund would derive its resources from the minimum — and free — deposits maintained with it by members. The overall amount of the minimum deposits, and their distribution

as between countries, would at all times adjust flexibly to the changes in each country's overall monetary reserves, and provide thereby the Fund with a pattern of resources directly related to the world demand for the various currencies needed for ultimate settlements. Finally, these deposits themselves would remain as fully liquid and usable for such settlements as gold itself and as the deposits now freely maintained by members in the form of currency balances in New York or in London. This was well described by an eminent expert as Lord Keynes, and need not be rehashed here (4).

As for Mr. Bernstein's proposed debentures, the effective resources which the Fund could ever derive from them would also — as in the case of the present currency subscriptions to the Fund's capital — be limited to a mere fraction of the amounts actually negotiated. Of the \$6 billion suggested by him, the \$3.5 billion to be contributed by the United States and the United Kingdom could not be touched as long as these two countries do not develop substantial surpluses in their balance of payments; and of the \$2.5 billion to be contributed by France, Germany, Canada, and "some other countries", only those amounts could be used which corresponded to the individual surpluses of any of the contributing countries (5). Once more, and exactly as for national currency subscriptions to the Fund's capital and capital increases, complex negotiations involving a large number of countries would end up in endowing the Fund with far lesser amounts of real, usable, resources than would appear at first view. Below the mountain of paper subscriptions and debentures, there would lie only a molehill of currencies actually usable for Fund lending.

#### IV. A Modest Initial Step

Yet, as radical a reform of the Fund as that proposed here is bound to require some time before it can be fully understood, appraised and negotiated. It will also have to surmount the enormous resistance which inertia, complacency and fears of anything new and unfamiliar, have always opposed to institutional progress, particularly in the international field.

(4) See the passages quoted in *Gold and the Dollar Crisis*, pp. 91-92.

(5) See his Joint Economic Study Paper No. 16, *International Effects of U.S. Economic Policy*, January 1960, p. 86.

A first, and very modest, step could be undertaken far more rapidly and simply, and yet be sufficient to achieve large results in minimum time. Let the International Monetary Fund declare its willingness to accept, on a purely voluntary basis, reserve deposits from member central banks. These reserve deposits would carry an exchange guarantee, earn interest to the depositors, and be freely usable to purchase from the Fund any currencies needed for international settlements. They could be acquired from the Fund against equivalent surrender of gold or of any balances in convertible currencies — primarily sterling and dollars — which the debtors of such balances agree to guarantee against the devaluation of their own currency and to amortize progressively, but at a *maximum* pace of, let us say, 5 per cent annually, insofar as deemed useful by the Fund for the proper conduct of its own operations.

The members' own interests should stimulate a considerable demand for such interest-earning, and yet exchange-guaranteed deposits. They would offer an attractive alternative to the massive conversions of dollar and sterling balances into gold, which have long been a major source of worry for the United Kingdom and have recently become an equal source of worry for the United States.

The keystone of such a proposal was endorsed *unanimously*, more than a year ago, by the Radcliffe Committee on the Working of the Monetary System (6). Agreement between the United States and the United Kingdom would practically guarantee the acceptance of this recommendation by the Fund. Other countries, indeed, could have no reason to oppose a step which imposes no obligation on them, but offers them, on the contrary, an additional and particularly attractive outlet for the investment of their monetary reserves. These other countries now retain, without any compulsion whatsoever, more than half of their reserves in national foreign currencies, always exposed to devaluation, inconvertibility, blocking, or even repudiation by the debtor. There is every reason to believe that no compulsion should prove necessary to induce them to retain as large a proportion, at least, of their reserves in the interest-paying *and exchange-guaranteed* deposits which would now be offered to them as an alternative.

This simple and immediately feasible measure might thus suffice to head off the crisis that could otherwise ensue from panicky

(6) See p. 248 of the *Report*.

conversions of dollar and sterling balances into gold. This would give central banks the time necessary to gain familiarity with the system, and to negotiate with greater confidence the more ambitious reforms necessary to consolidate it and to adjust the IMF and the international monetary system to the needs of our age.

May I, in closing, urge the reader to keep a sense of perspective in appraising the broad issues raised by my proposals and by Mr. Altman's criticisms. No human institution will ever be perfect and foolproof. The reforms which I suggest are certainly not exempt from a number of shortcomings, some of which — but not all — might be corrected in the process of negotiation. These shortcomings, however, should be compared with those of an international monetary system whose long term survival is admittedly impossible — at least beyond the five or ten years' reprieve optimistically granted it by Mr. Altman — and whose short-term functioning involves us right now in the most reckless and unnecessarily gambles about prospective gold production in South Africa, prospective gold sales by Russia in Western markets, the willingness of the key currency countries to supply reserves to the rest of the world through large and persistent deficits in their international payments and, last but not least, the continued acceptability of these countries' increasing flow of IOU's as a safe medium for the investment of their monetary reserves by the other countries of the world.

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#### APPENDIX

I would like to meet here a number of minor points raised by Mr. Altman, but some of which may be due to accidental misprints or cleared up by agreement on the exact meaning of some of the concepts and techniques used in his calculations:

1. Mr. Altman's guess in footnote 3, on p. 5, is perfectly correct. The 20 per cent criterion retained for compulsory reserve requirements was not uninfluenced by my hope that the coincidence which he notes would facilitate the acceptance of the proposed reform by the country which will have the largest voice in its negotiation.

2. The calculations mentioned in paragraph 11 (p. 5), paragraph 25 (p. 11), and paragraph 49 (p. 25) are based on the most pessimistic, but not necessarily most realistic, guess as to the relative attractiveness of gold and Fund deposits to the members of the reformed Fund. See p. 113 of my book. I would particularly object to the word « presumably » in the last sentence of paragraph 11 as representative of my thoughts on this matter.

3. The estimates quoted in paragraph 25 and footnote 1 (pp. 11-12) are somewhat garbled and partly ununderstandable to me. The deposit requirement of the U.S. should read \$4.5 billion, instead of \$4.1 billion. The \$2 billion of net claims on the IMF would be transformed into Fund deposits and raise by an equal amount the *gross* monetary reserves of the U.S. (see p. 13 of my book). Finally, \$3.5 billion of short-term liabilities to foreigners would be converted into long-term liabilities to the Fund. These calculations may be "controversial", but few people would hesitate to regard the net effect of these transactions as a "strengthening" rather than a "weakening" of the United States reserve position.

4. The increase in Germany's reserves was excluded by me, following Mr. Altman's own assumption in *International Reserves and Liquidity*, from the calculations of prospective reserve requirements discussed in paragraph 39 (p. 18).

5. The doubts raised by Mr. Altman at the end of paragraph 40 (p. 18) about the future reserve policies of the United Kingdom, and supported by his extensive footnote quotation from the Radcliffe Committee report, are not unreasonable. Let me note, however:

(a) that he rounds upward to \$5 billion the \$4.6 billion figure used in my calculations and quoted correctly by him in paragraph 4 (p. 2);

(b) that a \$4 to \$5 billion reserve target was repeatedly mentioned by the British in numerous official statements regarding the restoration of sterling convertibility;

(c) that my figure of \$4.6 billion is likely to be as close to a realistic reserve target for Britain as the one of \$2.2 billion implicit in the calculations of the Fund's report on *International Reserves and Liquidity*;

(d) that my estimate of \$2.5 billion for France is far closer to the current level of French reserves than the \$1.2 billion estimate of the same study.

6. I agree with Mr. Altman's criticism (in paragraph 40, p. 20) of the inclusion of IMF exchange assets in the estimate of world reserves used in my Wicksell lectures. This figure was borrowed somewhat hastily from the *International Financial Statistics*' own estimates of world reserves which might profitably be revised also, for instance along the lines suggested by Mr. Altman in paragraph 55 (p. 29). I cannot, however, quite reconstruct the derivation of his \$3.3 billion for *reserve* increases in this paragraph, unless he includes there non-official holdings of deposit money banks as reserves.

May I finally express some surprise at his use of my 1958 lectures in this sole connection, in preference to the more comprehensive and revised estimates used in my book and other more recent writings?

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