

# What Went Wrong? The Evolution of the IMF 1941-1961 \*

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## 1. Introduction

A remarkable series of Anglo-American discussions during the second world war reflected determination to prevent recurrence of the economic instability of the inter-war years. The outstanding result was agreement in July 1944 between a much wider group of countries, at the 'United Nations Monetary and Financial Conference' at Bretton Woods, in New Hampshire (USA) to establish the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development (the World Bank). Notwithstanding these striking endeavours, after a promising start in 1946-47 the new IMF was soon to cease, for almost nine years, to fulfil its expected role. To explain why this happened, in the wider context of international economic co-operation, is the concern of what follows.

Although financial problems dominated Bretton Woods, both the conference resolutions and the articles of agreement of Fund and Bank stressed the objective of fostering the growth of international trade, to improve employment and living standards. Subsequently, an international conference on trade and employment was held at Havana, Cuba. This reached agreement in March 1948 on a charter for a complementary body to promote those aims: the International Trade Organisation (ITO) (Cmd 7375, 1948). That never came into existence, but the General Agreement on Tariffs and Trade (GATT), intended as prologue to it, had been concluded in October 1947; it became

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a by no means insignificant instrument of trade liberalisation until agreement in 1993 upon a new World Trade Organization to encompass, when it commenced operations in 1995, broadly the more extensive responsibilities once envisaged for the stillborn ITO.

In contrast, the Fund and Bank were successfully launched in 1946. The Fund's specific functions were to oversee, and to provide short-term resources to support, a code of international financial behaviour. The Bank was to encourage and to provide international investment. The Fund, the principal concern here, soon seemed, however, to be sidelined until the Suez crisis of 1956. Two years later external convertibility for Western European currencies was restored, after almost twenty years: *de facto* at the end of 1958, formally early in 1961 under the Fund's Article VIII. This was clear, if as yet limited, recognition that the Fund was beginning to fulfil the purposes that its founders had intended.

In seeking explanations for this record of hope, disappointment, and revival, some questions first arise about the solutions that the designers of the IMF had sought for crucial problems raised by previous experience; their struggles to find answers illuminate subsequent difficulties.

## 2. Aims for a new international monetary system

Three sets of changes from pre-war conditions were considered:

- 1) Exchange rates should be realistic, reasonably stable, but adjustable without provoking competitive devaluation.
- 2) Countries needed adequate international reserves, and assured access to their short-term supplementation, to maintain convertibility in face of temporary economic fluctuations.
- 3) Codes of good practice in exchange rates and trade, overseen by international organisations, were necessary.

Questions arose on each of the *desiderata*, and on whether all three could be met simultaneously.

i) Were fixed rates the best answer? Had floating rates been demonstrably unsatisfactory? Had apparently unstable rates resulted from destabilising influences of other currencies?

ii) How far had inadequacy of international reserves reflected unrealistic exchange rates of surplus countries, and their hoarding of reserves? Did they intensify damaging deflation for debtor countries? Was the fault in the pre-1931 system itself, or in its restrictive operation by surplus countries? The latter was stressed by the British 'Macmillan Report' of 1931 on 'Finance and Industry', which Keynes had greatly influenced (Cmd 3897, 1931, paragraphs 246-48, 254).

iii) Did international cooperation have dangers? In the 1920s and 1930s it had propped up unrealistic exchange rates and encouraged a form of international liquidity undependable in financial crises; that was the gold exchange standard, by which some economies held all or most of their international reserves in foreign currencies, supposedly strong and gold-convertible (Table 1). If such reserve currencies were overvalued, they and dependent currencies were at hazard. That was the case with sterling from 1925 to 1931 and potentially after the 'Tripartite Declarations' of 1936, with American pressure on Britain for an over-valued five dollar pound (Drummond 1981). As for liberalised trade, would that be consistent with the fashion for domestic economic planning, for which trade controls might appear essential?

TABLE 1

FOREIGN EXCHANGE RESERVES  
(percentage of total reserves of 24 central banks, 1924-1932)

End of	1924	1925	1926	1927	1928	1929	1930	1931	1932
-	27	28	31	42	42	37	35	19	8

Source: League of Nations (1944, p. 235).

## 3. The background to proposals for monetary and trade reforms

Peacetime financial and trade relationships gave place, during and after the second world war, to new or intensified controls. To an exceptional degree, the devising of future monetary and trade arrangements involved academic experts dedicated to the elimination of such restrictions in all but exceptional circumstances (Ikenberry 1993).

Such discussions, when war had inevitably suspended normal trade and financial arrangements, created over-optimistic visions of world economic reform, which could flourish only briefly in that unreal atmosphere.

Apart from wartime euphoria about a better world, a dominating concern was to prevent the USA from slipping back into pre-war isolationism. In wartime it was Britain's chief paymaster; subsequently, its financial help was needed for economic recovery. The US was also prospective paymaster of whatever international financial institutions might emerge. Lord Keynes, the British government's free-ranging economic adviser and economic negotiator, was well aware of the sombre prospects for Britain's post-war balance of payments, and its dependence on special aid from the USA. He stressed that although there would continue to be fierce arguments with the US over trade policy, Britain must avoid irreconcilable opposition, and could not adopt a non-American commercial policy.

To leave no doubt on this, after Lend-Lease had commenced in Spring 1941 the American State Department soon presented the 'invoice' for that indispensable aid: a commitment was required from Britain to work with the US towards elimination of trade restrictions, especially discrimination, and in particular Britain's system of imperial preference, extensively developed since 1932. This commitment was embodied in a crucial and bitterly contested part ('Article VII') of the Mutual Aid Agreement of 1942 between Britain and the US:

"In the final determination of the benefits to be provided to the United States of America by the Government of the United Kingdom in return for aid [...] the terms and conditions [...] shall include provision for agreed action [...] directed to [...] the elimination of all forms of discriminatory treatment in international commerce and to the reduction of tariffs and other trade barriers" (Cmd 6341, 1942).

Should Britain have avoided this commitment? *Could* it have avoided it? The answer must be "No". Lend-Lease and active strategic involvement of the US in post-war Europe, as well as in financing British recovery, all mattered more.

#### 4. Keynes's Plan and White's Plan, 1941-1944

To accommodate Britain's economy to the obligations of Article VII, Keynes proposed an International Clearing Bank – later 'Union' (ICU). Circulated in draft in September 1941, it was published, after intensive discussions, in April 1943 (Cmd 6437, 1943). It was to be largely superseded, as the reference document leading to Bretton Woods, by the US proposal for a more limited Stabilisation Fund (SF). That was devised quite separately in the US Treasury, under Mr Harry D. White, from the end of 1941 following Pearl Harbour. By April 1944, transatlantic debate had transmuted the two proposals into 'The Joint Statement of Experts on the Establishment of an International Monetary Fund' (Cmd 6519, 1944a). That evolved in turn, three months later, into the Bretton Woods Agreements to establish the International Monetary Fund (IMF) and World Bank (Cmd 6546, 1944b).

Keynes had described his scheme as 'Utopian'. It sought to encompass in an ideal system the financing of trade and of its liberalisation; post-war reconstruction finance; development finance, possibly through a special Investment Board; and, it seemed, anything else requiring international finance. These were categories of needs, not exact prescriptions.

Britain's war-time government authorised use of the ICU proposal in non-committal discussions with the US, as offering a preferable alternative to autarky and austerity after the war. Eventually, the ICU's main emphasis was monetary. The possibility of an investment bank was maintained, but proposals for trade liberalisation were hived off.

Keynes argued for stable exchange rates, adjustable almost routinely according to reasonable rules. Ample liquidity should avoid the disastrous pre-war asymmetry in international payments, by which surplus countries had imposed painful adjustment on deficit countries. More abundant liquidity should also reduce temptations for deficit countries to restrict trade. The relevant international institutions should be very simple, Keynes was to urge; he was to continue to urge this up to the last minute at Savannah, Georgia, but unsuccessfully, against proposals for elaborate and expensively staffed institutions when in 1946 the IMF and the World Bank were formally established.

The ICU was envisaged by Keynes as self-equilibrating. A "mutual credit pool" (Viner 1951, p. 198) would be created by deficit

countries' drawing on the ICU, and thereby indirectly on surplus member countries. The pool of resources on which the former could draw would be provided by the latter's surpluses. Both surplus and deficit balances would incur interest charges, designed to give a bias against surplus members. There would be sanctions: prolonged deficits could justify voluntary or recommended devaluation by a small amount, while prolonged surpluses might evoke *instruction* to appreciate, and the forfeiture of excess balances.

"Perhaps the most difficult question" would arise here, Keynes recognised: "to determine how much to decide by rule and how much to leave to discretion" of *both* member countries and administrators of the Clearing Union (Keynes 1980, pp. 116-17). This was indeed a major trip-wire in constructing the proposed new international institution.

As if in response to Keynes, the American plan for a Stabilisation Fund was more constrained:

1) exchange rates should be stable, and fixed by the SF. Changes, allowable if there were a fundamental disequilibrium (nowhere clearly defined), would require approval by a majority of members.

2) Whereas in the ICU liquidity would arise in the form of claims on it, created by debtors or by the managing body, the SF would provide liquidity from subscriptions in gold and currencies. Resources would be smaller: eventually one-third of those implied by Keynes, with availability more complicated and somewhat more restricted. Further, whereas the ICU was to be largely passive, the SF was envisaged as active in currency markets. That was a disturbing prospect to the Bank of England, which, expecting difficult problems after the war, wanted to protect sterling from such unwelcome intervention (Fforde 1992).

3) Offsetting these narrower proposals were two potential *douceurs*:

a) a proposal, eventually abandoned but initially attractive to Britain, to fund accumulated balances owed to other countries.

In view of the immense volume of sterling balances, the management and re-payment of which were a serious constraint on Britain's balance of payments and economic policy after the war, Britain may have lost here a rare opportunity to reduce post-war strains on sterling.

b) in later drafts, a 'scarce currency' clause envisaged discrimination against a currency declared scarce by the Fund. Technically, however, this referred not to overall world scarcity of a currency but to the Fund's holding of it. This clause nevertheless proved a powerful incentive to accept the Fund.

## 5. Anglo-American monetary and trade discussions, 1942-1945

Differences between the Keynes and White plans were largely resolved *before* Bretton Woods during some two years of international discussions. By contrast, complementary trade proposals, after a promising start in 1943, were temporarily set aside and then diluted.

An 'International Commercial Union', the inspiration of James Meade in 1942-1943, proposed automatic rules to govern international trade, an expansionist policy, and drastic cuts in trade restrictions (Meade 1988, pp. 27-35 and 36-66; Gardner 1956, ch. 6; Cairncross and Watts 1989, pp. 99-103 and Pressnell 1987, pp. 100-01). A challenging response to that worrying Article VII of the Mutual Aid Agreement for Lend-Lease, it advocated across-the-board multilateral action, instead of the piecemeal bilateral bargaining that had hitherto characterised US policy, under the Reciprocal Trade Agreements Act of 1934.

Trade and monetary objectives were now, if briefly, considered in parallel, notably in remarkable discussions during September-October 1943, when a British team visited Washington. 'The Law Mission' (its leader was Mr Richard Law, a British Foreign Office Minister) included Meade, Keynes, Professor Lionel Robbins, and senior officials. The extensive discussions with US experts and officials were held "in the spirit of a university seminar rather than of a formal international conference" (Gardner 1956, p. 104).

Initially substantial harmony seemed to have prevailed on Meade's scheme, which provided the agenda on trade policy. A resulting series of documents embodied 'The Washington Principles' relating to general trade policy, commodities, cartels, and employment (summarised in Pressnell 1987, pp. 390-96). Within weeks, however, protectionist hostility from both sides shattered hope. For over a year,

Anglo-American discussions on trade policy were virtually suspended, to be resumed in December 1944 but within dispiritingly narrower constraints (Gardner 1956, ch. 8, and Pressnell 1987, chs 5 and 8).

Perplexingly, the recent official history of the IMF overlooks all this. Its distinguished author erroneously asserts the existence of a "wartime consensus that trade should not be debated", and that not until "well after the end of the war" in 1945 was there any initiative from the US (let alone by Britain) for an international trade organisation (James 1996, pp. 29 and 53). This unfortunately neglects the exceptionally important Anglo-American discussions of 1943 and 1944-1945, which influenced post-war endeavours to create a new international trade organisation. Apart from the record, the alleged absence of serious transatlantic debate must, indeed, seem *prima facie* inconceivable, given the momentous British commitment under Lend-Lease to work with American trade policy after the war.

## 6. The joint statement of 1944

Anglo-American discussions to reach agreement on monetary objectives continued after the Washington 'seminar' of September-October 1943. Wider consultations involved allied governments-in-exile as well as British Commonwealth governments (Keynes 1980, pp. 206-15, 239-41, 257). By April 1944 Anglo-American agreement had been achieved on a 'Joint Statement by Experts on the Establishment of an International Monetary Fund' (Cmd 6519, 1944a and Horsefield 1969, III, pp. 128-35).

The Joint Statement broadly followed SF rather than ICU lines. It leaned towards the ICU, however, in seeking to allay fear of interference with domestic policies: it would rely on responsible behaviour by member countries, not just on that of the prospective Fund's administrators. Three features were particularly noteworthy:

1) there would be greater scope for adjustment of exchange rates on the initiative of members. Grounds for Fund approval would explicitly exclude consideration of a country's "domestic social or political policies" (Cmd 6519, 1944a, IV (3)).

2) On provision of liquidity, which would come from subscriptions and be much smaller than envisaged by ICU, the Joint Statement's wording was to be virtually unchanged in the final Bretton Woods agreement. It allowed ample scope for interpretation in what eventually became the crucial issue of 'automaticity' of access. "A member shall be entitled" to acquire liquidity, provided that it be needed for payments "consistent with the purposes of the Fund".

This wording reflected an attempt to allay fears that the proposed new institution might exercise its authority in excessively discretionary fashion. The SF had originally envisaged "wide discretionary and policing powers" akin to those of central banks over domestic banks. Keynes (1980) had noted that:

"it may seem alarming to entrust any wide measure of discretion to a new body which necessarily starts without traditions [...] Our object must be [...] to limit [the] initiative and discretion [of those responsible for daily management] to cases where the rules and purposes of the institution are in risk of infringement [...]".

In the 1943 talks the American participants had recognised, however, the "undesirability of starting off" in that manner, and that member countries should have "as much certainty as possible" about facilities to be expected (Keynes 1980, pp. 404-05).

3) Transitional arrangements, before members fully implemented proposed obligations, had been neglected in ICU. The SF had proposed originally a transition of one year, subsequently three years, from its establishment. That now proposed would be relatively open-ended; member countries would simply be required to consult the Fund, within three years of its inauguration, about continuing restrictions.

The next and culminating stages in the evolution of the IMF were a working transatlantic voyage of British and allied experts; then a preliminary conference of representatives from sixteen countries in Atlantic City; and finally the major international conference in July 1944 at Bretton Woods (New Hampshire), in the appropriately named and situated Mount Washington Hotel, set against the White Mountains.

## 7. Atlantic City and Bretton Woods, June-July 1944

At Atlantic City the British sought further refinement of the monetary proposals. There was broad agreement on the proposed Reconstruction Bank. A major British accomplishment was American acceptance in the Fund's proposed articles of agreement of a clause that had been pressed in London by Lord Catto, newly Governor of the Bank of England and previously the financial adviser to the Chancellor of the Exchequer. This affirmed a country's ultimate sovereignty over its exchange rate. The US resisted, however, British attempts to extend the transition period. More ominous for the Fund's future was American resistance to automaticity in access to Fund resources (Horsefield 1969, I, p. 84).

On to Bretton Woods, where three relentlessly intensive weeks produced a text differing little in spirit from the Joint Statement. Two decisions had wide implications for the Fund's resources and eventual operation, though affecting Britain specifically. The first concerned the huge accumulated sterling balances, for whose repayment Indian and Egyptian holders sought conference support. In a delicately balanced debate, Keynes largely defused passionate feelings by delivering, on behalf of the British government, what became known as 'the Keynes pledge': that the balances would all be repaid. That removed a massive potential demand on the resources of the nascent Fund, and protected Britain from international meddling, at the cost of fixing a formidable burden on to its post-war economy.

The second item was the transition, on which the US now yielded. After three years countries need only report to the Fund on restrictions, and after five to consult it. The effective extent of the transition therefore had a degree of vagueness.

Did the proposed Fund meet Keynesian aims? Exchange rates were to be stable but adjustable, though with margins prescribed by the Fund. The buffer stock of available currencies was smaller than desired. The transition, however, seemed accommodatingly flexible. Capital controls were allowable to minimise disturbances from speculative movements. The scarce currency clause seemed a guarantee against extreme deflation.

## 8. Implementing Bretton Woods

The proposed IMF looked neat and orderly; would it work? Why impose an untried scheme? Would it not be better to approach it by stages, from existing proven arrangements? That was the view of the Bank of England, the successful manager of a network of wartime bilateral payments agreements. With adaptations these could – and indeed were to – support sterling after the war. The Bank's view, however, carried insufficient weight in 1944-1945, and not simply because, as a central bank, it was seen to be reluctant to surrender authority. The British Treasury recognised that it would be necessary to seek substantial post-war aid from the US. Not only was the Bank opposed to that, but its alternative of bilateralism was certain to antagonise the US and imperil Anglo-American relations (Fforde 1992, ch. 2).

Might the more compatible 'key currency' approach, advocated by Professor John H. Williams of Harvard and of the New York Federal Reserve Bank, have made better sense, as a transitional policy, than early implementation of the Bretton Woods proposals? This approach echoed the pre-war gold exchange standard, but with the greater security of being within the proposed new international arrangements. Initially, major currencies would accept rigorous requirements for stability. Other currencies would do so only gradually, meanwhile seeking stability through international co-operation and, inevitably, through the influence of the major currencies (Horsefield 1969, I, pp. 17-18 and 37; III, pp. 124-27).

This half-way proposal evoked British and American objections. It implied discrimination between members of the projected institution, and might be viewed as an attempt to secure Anglo-American dominance of it. Further, sterling would be a key currency, but there was fierce US antipathy to the existing example of the British sterling system, with its satellite currencies and discriminatory exchange controls. Harry White, in his advocacy of Bretton Woods, arbitrarily dismissed sterling's significance by simply ignoring the one-third of world trade, additional to Britain's, that it financed. He could then assert that the sterling-financed proportion consisted just of Britain's fifteen percent (instead of almost one-half). Taking account of the USA's twelve percent of world trade, there would remain seventy-odd

percent, for which the new Fund and Bank would offer stability (White 1945, p. 206).

Soon, American politics if not brutal economic reality brought implicit retreat from this statistical crudity. After vigorous debates, the US Congress approved the Bretton Woods agreements roughly a year after the conference. The next question was: how soon might the IMF begin operations? In mid-1944 the war seemed likely to last two more years; then there would be the extensible transition period. Within weeks of congressional approval, however, the sudden end of the war in August 1945 made activation of IMF, and the transition, immediate issues. Peace also brought to Washington a British mission seeking post-war aid of billions of dollars.

The Anglo-American financial agreement of 1945-1946 (Cmd 6708, 1945a), for a huge credit to assist Britain's post-war recovery, implied reversal of American hostility to the key currency approach in respect of sterling (Gardner 1956, p. 244). This was based partly on expectation that the threat to sterling's international usefulness, from accumulated excess balances, equivalent to about two years' imports, would be eased: at least until the IMF somehow took over.

The British loan had seemed to run counter to assurances to Congress before approving Bretton Woods in 1945, that further requests for special dollar loans to aid reconstruction abroad were not contemplated. Nevertheless, a year later congressional approval was being sought for the British loan. Adroitly, the US Administration coupled early implementation of Bretton Woods with support of sterling as a key currency, and joined to them the prospect of early trade liberalisation. In return for \$3.75 billion the British would renounce the transition of five years secured at Bretton Woods, in order to make sterling convertible after one year. This early convertibility of a key currency would not only accelerate activation of the new IMF, but also, with stringent conditions for the credit, offer better prospective value for dollars than those provided through the Fund (Gardner 1956, pp. 140 and 243-45).

British agreement to renounce the longer transition, and to eliminate restrictions on current payments within a year of the loan's ratification, was to be implemented in mid-July 1947. Even earlier, at the end of 1946, discrimination against US trade was to cease. These moves towards American policy were weakly reinforced, on conclusion of the financial agreement, by unenthusiastic British support

of American proposals for a conference to establish an International Trade Organisation (Cmd 1945b; Pressnell 1987, pp. 326-29).

As with Bretton Woods, Congress was assured that the request for aid dollars would not be quickly repeated. So declared Mr Will L. Clayton, Assistant Secretary of State for Economic Affairs, a Southerner of great probity (Gardner 1956, pp. 95-96 and 245). Nevertheless, within eighteen months, by which time US scrutiny of overseas assistance was tightening, he would be seeking even more massive amounts of dollars. This time it was for Marshall Aid. The grant of that would provide an opportunity to strengthen US influence in the IMF, as will shortly appear.

The Bretton Woods agreements had to be ratified by the end of 1945. Twinned with the financial agreement of 6 December 1945, it was rushed through the British Parliament before Christmas. Within a few months the Fund was formally launched, in March 1946. Most member countries had declared initial par values by the end of the year. Formal operation commenced in March 1947. Of the principal members, only the US acceded to the key Article VIII, with commitment to avoid restrictions on current payments and on creditors' accumulated balances; there would be a long wait for further major accessions (Table 2).

TABLE 2

## ARTICLE VIII ACCESSIONS, 1946-1961

1946	El Salvador, Mexico, Panama, US
1947	Guatemala
1950	Honduras
1952	Canada
1953	Haiti
1961	Belgium, France, F.R. Germany, Ireland, Italy, Luxembourg, Netherlands, Peru, Saudi Arabia, Sweden, UK

Source: IMF, *Annual Report 1965*, p. 107.

## 9. International trade proposals, 1943-1950

If the post-war monetary plans were being implemented in 1946-1947, what was happening about trade reforms intended to complement them?

Following the retreat from the 1943 understandings discussed earlier, reassessment had delayed consensus. A conference resolution at Bretton Woods nevertheless urged national policies on post-war trade to work to similar ends. The first Article of the IMF agreement stressed its aim as "the expansion and balanced growth of international trade", to facilitate high employment, high real income, and economic development. The first Article of the World Bank agreement embodied comparable affirmations.

A common myth notwithstanding, the conference did not, however, advocate the eventually aborted International Trade Organisation, which the US did not propose until December 1944. American and British aims on trade policy, in many respects comparable, diverged strongly on the fundamental issue of discrimination. British support for international oversight of trading practices was to become increasingly qualified. The US consistently sought reduction of tariff barriers, avoidance of quantitative restrictions, elimination of discrimination under trade preferences – though, awkwardly, not their own for Cuba and the Philippines (Gardner 1956, pp. 353-54) – and a charter of enforceable trading rules. British objectives included tariff cuts to permit greatly expanded exports, but defence of imperial preference against fierce American hostility: less on its merit than as a bargaining chip not to be traded for scant returns.

For a year from the end of 1944, Anglo-American discussions on trade policy centred around the American proposal for a Convention on commercial policy. This was intended to establish the ITO (Pressnell 1987, pp. 200-11). It was well short of a compromise, such as 'The Joint Statement' preceding Bretton Woods had been. In three respects it seemed loaded against British concerns:

1) tariff cuts appeared adequate neither for trade expansion, nor to compensate for cuts in preferences, which, indeed, the US strove to eliminate without compensation.

2) The accumulated sterling balances, the Americans feared, would encourage discrimination favouring trade with their holders.

American policy was that such balances should be convertible, and that discrimination should require consultation with the proposed ITO. The first aim would have imposed unacceptable burdens on sterling, hampering multilateral trade. The second aim would have involved international surveillance, additional to that by the IMF, possibly jeopardising prospects for British approval of the Fund itself.

3) Alarming, the proposals embodied tighter constraints than the IMF agreement. After five years, instead of consultation about restrictions (Cmd 6546, 1994b, XIV), they would have to be terminated. This proposal for a more rigorous transition was made even before a much shortened transition was required by the Anglo-American financial agreement of 1945-1946.

Yet more worrying was the American retreat by mid-1945 from the multilateral approach inspiring Meade's proposal of 1942-1943 for a 'Commercial Union'. Congressional apprehensions were adduced for reversion towards bilateral negotiations. Consequently, as noted above, at the end of 1945 there was only hesitant British support of US proposals for an international conference on trade and employment.

In the preparations for the culminating Havana Conference on International Trade and Employment, of December 1947-March 1948, which agreed on a charter for an International Trade Organisation (Gardner 1956, chs 14 and 17), the major outcome had been the General Agreement on Tariffs and Trade (GATT) of 1947. Its all-round tariff reductions signalled, to American eyes, liquidation of the notorious Hawley-Smoot tariff of 1930, and tariff levels lower than under their relatively moderate tariff of 1913 (*FRUS* 1947, I, pp. 976 and 989-90). Britain refused major concessions on preferences, but had to agree that the proposed ITO should have power from March 1952 to request removal of trade discrimination. At the Havana Conference, however, so many exceptions had been made to the lifting of trade restrictions that its charter proved unacceptable to the US Congress, from which the US Administration withdrew it at the end of 1950 (Gardner 1956, p. 378).

The GATT remained: a less powerful but acceptable substitute for the ITO. Its provisional character, flexibility and lack of prescriptiveness compared for many reassuringly with the Fund's tautening



conditions from 1948. Indeed, the Fund was concerned not only lest GATT stray into its own remit, but also that it should not appear to offer escape routes from it. The Fund was represented at various GATT conferences and, reflecting provisions in the draft ITO charter, established regular relations with GATT; it provided information, in connection with projected or existing trade restrictions, on the balance of payments of members. For contracting parties of the GATT, which were not members of the Fund, 'Special Exchange Arrangements' involved obligations, in respect of exchange and trade restrictions, corresponding with those required of Fund members (IMF/AR 1947, p. 38; Horsefield 1969, I, pp. 171-75 and 290-92, and De Vries in Horsefield 1969, II, ch. 16).

#### 10. The IMF in operation 1947-1961: guidelines for drawing

For all too brief a time, in its first year or so, the Fund appeared likely to fulfil the more optimistic hopes of uncomplicated access to its assistance. In November 1946 the British Executive Director, Mr George Bolton of the Bank of England, saw no immediate reason to expect meddling in countries' domestic affairs. Some months later, when the crisis of August 1947 over the premature adoption of current convertibility for sterling led to British drawing on the Fund, a British Treasury brief for delegates to its annual meeting considered that the "battle for 'automaticity' may be largely regarded as won" (Dell 1981, p. 8).

In truth, that 'battle for automaticity' was already being lost. A more stringent attitude by the US towards the grant of dollar aid blended with a more qualified interpretation of Fund articles to restrict access to drawing facilities.

As the US, during the early months of 1947, contemplated increased international responsibilities and associated dollar assistance, unease already expressed in congressional interrogations over management of previous dollar aid stimulated a new determination to insist in future on strict scrutiny and surveillance. Shortly before Secretary of State Marshall's historic offer of substantial aid for European recovery in June 1947, this had been strikingly expressed in a definitive memorandum from one of its leading progenitors. Mr Will L. Clayton, Under Secretary of State for Foreign Affairs,

emphasised that "The United States must run this show" (*FRUS* 1947, III, pp. 197-219, 230-32 and 237-39).

Just ahead of that affirmation the Fund board had asserted, earlier in May 1947, its right to challenge a member's declaration of the need for a drawing. It might "postpone or reject the request, or accept it subject to conditions". This decision echoed American reservations about automaticity in June 1944, shortly before the Bretton Woods conference. It was to be confirmed ten months later, in March 1948 (IMF/AR 1947, p. 31; 1948, pp. 97-99; Horsefield 1969, I, p. 189; II, pp. 385-86; III, p. 227).

The implications of Marshall Aid for the Fund were already being examined at the beginning of 1948, under prompting from the US Administration. Although discussions pointed to closer evaluation of requests to draw by recipients of Aid, fuller consideration and decision came later. In April, two days after Congress had approved the ERP, the Fund resolved that, at least initially, recipients of Marshall Aid should not expect, other than in abnormal circumstances, to be able also to acquire dollars from the Fund:

"For the first year the attitude of the Fund and ERP members should be that such members should request the purchase of United States dollars from the Fund only in exceptional or unforeseen cases" (IMF/AR 1948, p. 74).

It was not, however, this 'ERP resolution' but the recently re-affirmed, more demanding interpretations of eligibility to draw that, in the view of (Sir) Joseph Gold, the Fund's General Counsel, caused "almost complete paralysis" of its financial operations (Gold 1969, p. 523, and Table 3 below, p. 234). Over the next four years, the evolution of 'conditionality' discouraged resort to the Fund, the status of which, its intended role, and therefore, indeed, its survival were in question.

#### 11. Did member countries distrust the IMF?

That this decline was attributable largely to Fund decisions, albeit under US pressure, seems evident, but did it also reflect lack of confidence in it? The latter possibility arises in respect of two particu-

lar sources of unease: the Fund's unpropitiously early start, and actions by some leading countries in the difficult years from 1948 to 1950.

After the 1939-1945 war several years were needed, as after earlier major wars, for economic recovery. Was therefore the IMF launched prematurely, just a few months after that war had ended? In anticipation, rigorous American policy-makers had asserted that a prolonged transition would tempt war-damaged economies to 'run wild', perpetuating restrictions and unacceptably delaying operation of new monetary and trade disciplines (Anglo-American trade policy discussions, 11 January 1945: PRO, CAB 123/96-I). The collapse in less than six weeks, during summer 1947, of the British attempt to operate both general convertibility for sterling and non-discrimination in trade provided a brutal response. It is not clear, however, that this damaged the Fund's underlying rationale.

What of actions by individual member countries that have been regarded as weakening the new IMF? Four may be considered: by Britain in 1947 and 1949, France in 1948, and Canada in 1950.

The last, with the direct challenge by the floating of the Canadian dollar to the Fund's crucial commitment to fixed exchange rates, can be dismissed first and quickly. The Fund recognised it as a well-intentioned and temporary reaction to speculative inflows, and was subsequently to express satisfaction with experience in the early months of floating (Horsefield 1969, pp. 273-74).

Earlier, the collapse of sterling convertibility in 1947 had discredited less the new international system than those responsible for predictable disaster. Damage to sterling was more significant than any to the IMF, as British Treasury officials ruefully learned when subsequently re-negotiating recently concluded financial agreements.

A few months after sterling's crisis, France devalued massively in January 1948, with multiple rates for hard currencies. Unsuccessful attempts at dissuasion had been made by the Fund, and also directly by Britain, apprehensive that sterling's parity would be undermined (PRO, T 236/902, FO 371/68980-2; Fforde 1992, pp. 223-24). Unlike Italy, whose elaboration of existing multiple rates the Fund had accepted, France had not hitherto operated such a system. The Fund declared it ineligible to use its resources. This outcome scarcely looks like a discrediting of the Fund (IMF/AR 1948, pp. 63-64 on Italy and pp. 37, 76-78 on France).

Finally, there is an entrenched assumption that Britain's devaluation of sterling in September 1949 displayed scant regard for the Fund as well as for other European countries. This overlooks antecedent pressures on sterling, and confuses indignation with reality.

When initial par values were notified in 1946-1947, with recovery far from complete, they were recognised to be non-equilibrium rates, and likely to be readjusted. From early 1948 there was widespread international discussion of the need for European devaluations, especially of sterling, still a 'key currency'. The Fund's Executive Board actively considered 'European Exchange Rates' from March 1949 (IMF/AR 1948, pp. 22-24; 1949, pp. 9-16; Horsefield 1969, I, pp. 218 and 234-37). Only the timing and extent of devaluation could merit surprise.

The speculative hazards for sterling need no elaboration. They became alarming during late March-early April 1949, when US representatives in the Fund pressed successfully a resolution which urged "attention to [...] existing exchange rates" (Horsefield 1969, I, pp. 234-35). Intensive British efforts had only slightly diluted the April resolution (Fforde 1992, pp. 282-83). So far it was sterling under attack: not the Fund. From Britain a damage-limitation team flew to the US to remonstrate that American pressure, inciting "a full-blooded 'bear' attack on sterling", was distorting the Fund's intended mission from stability into instability. US prescriptions would make it "extremely difficult to see what advantages were to be obtained from membership of the Fund" (PRO, CAB 134/222, EPC(49)63; *FRUS* 1949, IV, pp. 781-84; Cairncross 1989, pp. 58-63).

When Britain finally decided on sterling's devaluation, the Fund had to be informed first; next, in strict confidence shortly before the public announcement, certain other countries were told. Against subsequent continental resentment and portrayal of British behaviour as high-handed stood that obligation to the Fund, as well as justifiable fear of leakages. Mr Dean Acheson, US Secretary of State, considered that "All went well" bar the supposed failure to give prior notice to the French; in fact, their Finance Minister was informed beforehand. As for the Fund its official historian stresses that formalities had been observed, and denies that it had been "a mere rubber stamp for governmental decisions". Representation on its Board ensured that "at every stage in the policy-forming process [...] Governments were kept informed of the views and plans disclosed". At the very least, he

concludes, the Fund had facilitated relatively orderly adjustment of rates (Acheson 1970, p. 325; PRO 1949, Fo 800/465, telegram 4487 of 16 September 1949, Washington to London; Horsefield 1969, I, pp. 241-42).

## 12. The Fund's evolution of 'conditionality'

US determination to strengthen control of its IMF dollars had been expressed early in 1948, not only by the 'challenge' on drawings and the ERP decisions of 1947-1948, but also when the American Executive Director enunciated four criteria for drawings: the appropriateness of the existing exchange rate, repayment prospects, appropriate short-term purposes, and satisfactory monetary and fiscal policies. Before long the British Executive Director was complaining of "obligations but no benefits". But more was to come, when in spring 1949 the US reinforced its criteria: in particular, that would-be borrowers should be doing their best to move rapidly towards full assumption of Fund obligations (Horsefield 1969, I, pp. 224 and 242-45).

That this increasing rigour diminished the Fund as well as member countries was sadly evident. Despite its Managing Director's protest early in 1951 against "the current tendency to write off the Fund as moribund", activity continued low into 1952-1953, with staff morale suffering (Horsefield 1969, I, p. 336). New prospects, however, were already in sight.

## 13. A fresh start from 1951-1952: the Rooth Plan

Under a new Managing Director, Mr Ivar Rooth, emphasis shifted during late 1951-early 1952 towards facilitating greater use of the Fund, although it was realised that this would take time to succeed. The background was propitious, however, in two respects. The 'ERP decision' of 1948 lapsed as Marshall Aid ended in 1952. At the same time the transitional period of five years, since commencement of Fund operations, ended; annual consultations were now required with members about exchange restrictions. If the first made

better relations between Fund and members possible, the second made them particularly desirable.

'Automaticity' in access to Fund resources was at last approached in respect of drawings on the gold tranche: the first quarter, subscribed in gold, of a member's quota. The rotating character of Fund resources would be strengthened by charges revised to encourage repayment and therefore relatively short-term borrowing. The establishment of 'standby' facilities was eventually to stimulate wider resort to the Fund.

The principles underlying these and other changes were elaborated in the 'Rooth Plan' of February 1952. Phrased more sensitively than some earlier Fund statements, its aim was "to provide a practical basis for use of the Fund's resources in accordance with the purposes of the Fund". Its constructive approach emphasised closer attention to members' needs for assistance and for fuller discussions. This was indeed "the Mount Everest that towers over all other decisions on the use of the Fund's resources": albeit a mountain requiring a few more years to climb (IMF/AR 1952, pp. 87-89; Horsefield 1969, I, pp. 323-25, 329-30, 490-91; III, pp. 228-30; Gold 1969, pp. 523-24).

## 14. The revival of the IMF: the Suez crisis of 1956, quota increases and increased activity

As the Rooth Plan had stressed, the Fund's recovery would take time (an important aspect of this, its temporary overshadowing by the European Payments Union in the 1950s, is discussed in Section 15 below). Not until the Suez crisis of 1956 did it achieve recognition as a significant stabilising influence in international payments.

Following the Anglo-French military intervention in the Israeli-Egyptian conflict, speculative attacks seriously weakened sterling. In default of adequate aid, the floating of sterling would have been a drastic reaction by one of the world's two major currencies. To avert that Mr Per Jacobsson, the vigorous new Managing Director of the Fund, resolved that its resources should be used to defeat speculation. Overcoming technical obstacles in the Fund's Articles, Mr Jacobsson secured agreement on massive aid. He stressed that this was exceptional and not a precedent. He insisted, rightly in the event, that confidence was crucial; demonstration of Fund confidence in sterling

would settle markets and allow Britain scope to resolve its problems. A substantial British drawing was supplemented by an even larger stand-by credit, which did not need to be used, as well as by direct American aid (Jacobsson 1979, pp. 283 and 285; IMF/AR 1957, pp. 10 and 53-54; Horsefield 1969, I, pp. 428-29 and II, pp. 412-13).

TABLE 3

IMF FINANCIAL ASSISTANCE 1947-1948/1962-1963  
(fiscal years ending 30 April)  
Drawings, new standby arrangements and exchange transactions  
not effected under standby arrangements

Years ending 30 April	Country membership	Countries assisted	Total assistance (\$ million <sup>a</sup> )	Total quotas (beginning of year) (\$ million <sup>a</sup> )
1948 <sup>b</sup>	44	10	606	7,722
1949	46	10	119	7,976
1950	47	4	52	8,034
1951	47	1	28	7,922
1952	49	2	46	8,037
1953	51	6	119	8,154
1954	54	7	268	8,737
1955	56	3	49	8,849
1956	56	4	74	8,728
1957	58	13	1,986	8,751
1958	60	18	656	8,932
1959	67	13	346	9,088
1960	68	16	430	9,228
1961	68	22	856	14,277
1962	76	26	3,469	14,851
1963	85	22	1,839	15,057

<sup>a</sup> Rounded.

<sup>b</sup> From commencement of transactions, 1 March 1947 to 30 April 1948.

Source: IMF, *Annual Report* (various years); *Annual Report 1963* (Table 6, p. 24).

This assistance for sterling exceeded total drawings on the Fund in the previous nine years. Maintenance of the greater flexibility shown in the Suez crisis encouraged greater resort to the Fund, bringing it closer to the role envisaged at Bretton Woods. Annually over the next four years three times as many members as before the crisis were given assistance, the total of which rose correspondingly.

This was underpinned by increased resources. Quotas had effectively shrunk because of inflation and their lower ratio to almost doubled world trade. Members therefore faced more quickly the demanding requirements set for drawing higher credit tranches of their quotas. More dollars, it is true, came from outside the Fund as Marshall aid ended: in military aid, rising inflows of private short- and long-term American capital, and improved dollar earnings by European countries and others. Until the late 1950s, however, larger quotas proved unacceptable to the US, the main provider of Fund resources. When at last agreement came in 1959, quotas were increased by a standard fifty per cent, with special increases for certain member countries (IMF/AR 1959, pp. 13-15; IMF/AR 1960, pp. 13-14).

### 15. Trade liberalisation: the OEEC and the EPU

In moves by European countries, both in liberalisation of trade during the 1950s and to convertibility 1958-1961, the Fund's role was limited. Regular consultations with GATT, however, helped it to evaluate the balance of payments implications of diminished trade restrictions (De Vries 1969, pp. 345-46).

The main mechanisms improving European payments and trade were the Organisation for European Economic Cooperation (OEEC), and the European Payments Union (EPU). The former was the European body supervising Marshall Aid. The latter's principal function was provision of a regional clearing system, and limited automatic credit between OEEC members; it thus resembled a scaled-down version of Keynes's 'International Clearing Union'. A striking aspect of the EPU was that membership required adherence to a code of trade liberalisation, supervised at first by the OEEC's Trade Committee, and from 1952 by a special 'Steering Board for Trade' (Kaplan and Schleiminger 1989, pp. 82-83 and 94). To encourage liberalisation within the OEEC, the US tolerated continuance of discrimination against dollar trade; this accorded with the view, embodied in the abortive ITO charter, that expectations of longer-run benefits from regional integration, such as Marshall Aid was intended to promote in Europe, justified interim discrimination.

Liberalisation was progressively increased, though occasional modification or even suspension resulted from balance of payments

difficulties, notably during the Korean war. Its significance is not easy to assess; it was largely based on the volume and composition of private (not governmental) trade in 1948, and thus had incomplete coverage. Moreover, as quantitative restrictions, its especial concern, were relaxed, tariff barriers became more effective. Whereas reduction of the former may have increased intra-European trade, that of the latter was particularly needed to foster trade and payments equilibrium with the rest of the world.

That the IMF was not closely involved at the outset, in 1949-1950, in the evolution of the EPU's clearing arrangements, credit facilities, and associated liberalisation of trade must seem extraordinary. These were, after all, precisely its concerns; the existence of the EPU seemed, however, to diminish further the Fund's significance.

TABLE 4

LIBERALISATION OF INTRA-EUROPEAN PRIVATE TRADE, 1951-1959  
(quantitative restrictions; mostly on 1948 basis in %)

1951 June	1952 Oct.	1953 March	1954 April	1955 April	1956 April	1957 April	1958 Jan.	1959 Jan.
65	61	67.5	81	84	87	89	83	89

Source: BIS, *Annual Reports* (various years).

The Fund's non-involvement effectively dated from 1947, when the European response to the offer of Marshall Aid included a scheme for intra-European payments, for which it was proposed as the clearing agent. The Fund had been represented at initial meetings but not in later decisive discussions; this unintended absence was apparently due to administrative oversight within the Fund. The proposed task was therefore assigned to the Bank for International Settlements (Horsefield, I, pp. 214-15; De Vries 1969, p. 323).

By the time EPU was being shaped, however, there were underlying tensions. In the Fund views were divided: would the EPU's policies help or hinder achievement of European viability in dollar trade and payments? The Fund was perhaps more hesitant than if it had been a more mature institution, less uncertain of its international influence. Second, the OEEC and the EPU were wary about the Fund. Not only had there been that discouraging resolution of April 1948 as Marshall Aid was beginning: there was also strong resistance

to involvement of the more broadly international body in distinctively European matters.

These tensions fortunately lessened from about 1952. From the Fund came easements already noted. From the EPU came liberalisation in trade and payments that reflected the Fund's aims better than anticipated. Not least, there was cooperation over financial problems of mutual concern, as over negotiation in 1955 of the European Monetary Agreement, likely to be less competitive with the Fund, and of aid to France and Turkey in 1958 (Kaplan and Schleiminger 1989, pp. 41-43, 124 and 340; De Vries 1969).

## 16. Conclusion

From 1948 to 1961, experience of the IMF and GATT had fallen short of the more optimistic hopes of Bretton Woods in 1944. Progress towards achievement of at least a modicum of the three *desiderata* of orderly exchange rates, adequate liquidity, and observance of international rules in trade had often seemed elusive. Moreover, when much was nevertheless accomplished during the 1950s through the OEEC and EPU, the IMF was seen to be sidelined and, indeed, to have sidelined itself. For a few years its assistance became much less readily accessible than originally expected. By 1952, however, in contrast to its constraints of the late 1940s the Fund was evolving more flexibly.

Achievement of *de facto* external convertibility by major European countries at the end of 1958 occasioned their invocation of provisions for dissolution of the EPU. When in 1961 they formalised convertibility by adoption of Article VIII of the Fund, this marked significant movement towards the Fund's intended status as "the focal point of important monetary decisions" (Kaplan and Schleiminger, 1989, p. 317; De Vries 1969, p. 317).

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