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The IMF: The Second Coming?

In this essay I speculate on the future of the international monetary system in the light of its present crisis. I consider two *extreme* possibilities that could occur in the next few years. The more likely possibility would be a gradual return to Bretton Woods—but to a system in some respects more like the one planned in 1944 than the one that has emerged in recent years. This development would spell increasing integration of the world economy. At the other extreme, in the event of failure of the first, would be the division of the world into two or a very few monetary blocs that would be defensive in origin and therefore likely to lead to increased barriers to economic intercourse among the areas. I pay special attention, where appropriate, to the problems posed for the less-developed countries (LDCs) by the present situation and its development.

The first section briefly sketches the background of the crisis of August and the realignment of December 1971. The second section presents a suggestion for reshaping the international monetary system that might prevent future monetary crises and describes the steps by which the system created by the realignment could evolve toward this model. The third section draws some conclusions and reflects on possible further developments.

From Crisis to Realignment

The unilateral and formal suspension by the United States of dollar convertibility into gold on August 15, 1971, led at first to the widespread belief that the Bretton Woods system of stable exchange rates had finally collapsed and that the trend toward increasing international economic cooperation evident since the Second World War might be reversed. These fears were heardly surprising. The U.S. action had been preceded by a succession of increasingly severe monetary crises that had resulted, among other things, in the floating of major currencies, including, since May 1971, the Deutschemark. President Nixon had spoken of the need for a new international monetary system.

As an immediate result of the U.S. action, strategic rules of the international monetary system were put into suspense. Despite their legal obligations under the Articles of Agreement of the International Monetary Fund (IMF), member countries generally felt free to change the relationships of their currencies to the U.S. dollar and to each other. On the same day that the United States closed the gold window, it also

adopted or planned a series of exceptional measures to discourage imports and stimulate exports: an import surcharge, exclusion of imported capital equipment from the proposed "job development" (investment) tax credit, tax advantages for exports through domestic international sales corporations, and a cut in foreign-aid expenditures. The first two measures, it is true, were to be removed after an exchange-rate realignment, a new deal with allied countries on the sharing of defense costs ("burden sharing"), and an agreement with the major industrial countries on the removal of "specific trade barriers," provided these together yielded a strong balance of payments for the United States.

As the result of an unprecedented multilateral negotiation on exchange rates, by December 18, 1971, a new rate structure had already been agreed upon by the members of the Group of Ten—the countries associated in the General Arrangements to Borrow (more accurately, to lend to the IMF), including the United States, the United Kingdom, Japan, Germany, France, and five other industrialized countries, with which Switzerland is associated. By the end of the year, most IMF members had also indicated new exchange rates to the Fund. Thus, less than five months after the dollar went off gold, the period of discretionary floats seemed to be over (except for Canada and a few LDCs). The surcharge and the buy-American feature of the investment-tax credit had been terminated. Negotiations were under way to settle other questions of immediate concern.

The dollar remained inconvertible into gold, but its effective convertibility had been severely limited even before August 1971. Thus, for all practical purposes, the world seemed back where it had been—not in mid-1971, when the system was already disrupted by the floating of major currencies, but in mid-1970, when only the Canadian dollar, among the currencies of industrial countries, was floating. Yet all recognized that none of the underlying problems of the international monetary system had been solved. Whether the realignment can hold (subject only to orderly modification) or will collapse, and possibly reverse the trend toward increasing integration of the world economy, depends in part on whether necessary reforms of the international monetary system can be enacted in time. The mechanics of reform will not be decisive, but much does depend on the policy intentions underlying the enactment of reforms.

The Background

The basic deficit of the U.S. balance of payments had been rising for years. This deficit might possibly have been reduced to a rate that the world could tolerate even without an exchange-rate realignment.

Under conditions of relatively rapid growth of the world economy, a few years' relative wage and price restraint in the United States and only moderate price rises elsewhere might have produced the same effects as the realignment (which resulted in an average devaluation of the dollar by somewhat less than 9 per cent, compared with April 1970).

Such a solution, however, would have required assurances by other countries that they would not present existing dollar balances for conversion into U.S. reserve assets. Actually, in the weeks before August 15, 1971, U.S. reserve liabilities and losses of reserve assets had risen dramatically. It is also possible that there were indications of large future demands for the conversion of dollars into gold. The tacit agreement to refrain from such demands by which many major central banks had apparently been bound (in addition to explicit understandings with others) seemed to be at an end. Moreover, there may have been signs of a breakdown in the network of bilateral credits (swaps and others) by which major central banks were in the habit of assisting each other in difficulties and which had been used on a large scale by the United States.

The Realignment

The measures adopted or announced on August 15, 1971, could do little directly to improve the U.S. balance of payments and could do nothing directly to bring about the desired realignment. Essentially, each country (except the United States) determines the value of its currency in its own territory by *both* buying and selling it freely at the desired rate(s) in terms of dollars (i.e., using the dollar as "intervention currency"). Consistent rates against other currencies are maintained by private arbitrage operations. (A few countries use sterling or francs as their intervention currency or supply other currencies at consistent rates.) Under this particular system of intervention, the United States does not need to intervene, even in its own territory, to maintain the value of the dollar against any other currency. (Indeed it must not do so; between any currency and the remaining $N - 1$, there are only $N - 1$ independent exchange rates, and simultaneous intervention by all N authorities could lead to contradictions.) Convertibility into gold, in other words, is not needed to maintain the value of the dollar in terms of other currencies. Its function, if it had existed on a substantial scale in fact, not only in form, would have been, at most, to limit the ability of the United States to finance deficits (i.e., to "discipline" U.S. policy). The suspension of convertibility into gold could not by itself affect the foreign-exchange value of the dollar.

The suspension of convertibility could and did create an expectation

of revaluation of other currencies against the dollar, inducing the "Gnomes of Zurich" to force the respective monetary authorities to validate the expectation (if they could not ward off speculation by imposing controls or by intervention). By the beginning of December 1971, almost three-quarters of the eventual average dollar depreciation enacted formally in the realignment of December 18, 1971, had been accomplished, compared with exchange rates prevailing in April 1970, before the Canadian dollar was floated. (At the time the U.S. dollar went off gold, the floats and revaluations that had taken place earlier in 1971 had already achieved one-quarter of the eventual depreciation.)

The surcharge and the buy-American feature of the investment-tax credit made no direct contribution to the realignment. These two measures, in fact, limited market pressure for realignment. Nor was the promise of their removal an incentive toward it. Except for Japan, these measures hit heavily only countries from which little or no (further) revaluation or other action was expected—Canada and LDCs such as Mexico. Furthermore, given the damage to a country's exports caused by these measures, the promise to remove them was an economic incentive to revaluation in inverse proportion to the extent of the (further) revaluation desired from each country: the larger the desired additional revaluation, the more painful it would be compared with continuation of the measures. Finally, few of the major countries suffered acutely from the exchange-rate uncertainty—least of all, of course, the United States itself. Thus there was little direct economic pressure on other countries for further appreciation or on the United States to agree to a degree of dollar devaluation (in terms of gold and foreign currencies) acceptable to those other countries.

What did bring about the additional realignment was, in part, political pressure on the countries whose rates had moved least by those that had already "done their share" and wanted to diminish competition from the laggards. More important was the fear in one or more countries, Germany among them, that recessionary tendencies, even if slight at the moment, might be strengthened by the persistence of the prevailing uncertainties. The United States presumably also realized that such a development would make any further realignment progressively more difficult. The major reason for agreeing on an early realignment, however, was fear that the unsettled situation resulting from delay might lead to the proliferation of measures that would reverse the movement toward increasing integration of the world economy. The surcharge and the buy-American feature of the investment-tax credit were signs of the direction in which policies might move and in this sense only may have contributed to the realignment. No government,

it should be stressed, seemed prepared to opt for the alternative form of agreed solution—a *commitment* to freely floating rates.

The realignment left no country completely satisfied. The United States had wanted a realignment which, together with the other concessions it demanded of the Group of Ten, would have improved the full-employment equivalent of the U.S. current account by $13 billion in 1972, had the realignment and other measures been in force long enough to have taken full effect. The United States apparently thought an average devaluation of the dollar close to 15 per cent was required to bring about this swing, which was considered necessary to compensate for the prospective net capital and aid outflow and to provide a margin of safety. The actual realignment was close to 9 per cent, but market rates will be allowed to fluctuate between wider margins than in the past. Thus the realignment alone could perhaps produce a swing approaching $11 billion, to which would be added the effects of the other concessions. As part of the realignment, the United States promised to propose to the U.S. Congress a devaluation of the dollar in terms of gold by 7.89 per cent, as soon as agreement had been reached on the other concessions. It had at first opposed this devaluation for political reasons and because it feared a possible adverse effect on the willingness of private individuals to continue holding dollars. A few European countries had insisted on it, to ease the political problem they would face of appreciating vis-à-vis the dollar and to compensate them in part for losses in the purchasing power of the dollars they held as reserves. The United States made no commitment to resume convertibility of the dollar in any form, but agreed that establishment of a "proper degree of convertibility of the system" should be studied in the context of a long-term reform of the IMF. The Group of Ten, other than the United States, had wanted a small realignment and a small swing in the U.S. current account. Many felt that the requisite improvement in the over-all balance of payments should be achieved partly on capital account, by U.S. restrictions on direct investment in developed countries. Some felt that the appreciation to which they had agreed for their own currencies had been inequitably large, not vis-à-vis the dollar but vis-à-vis other currencies of the Group of Ten.

The leading role taken by the Group of Ten in the realignment was somewhat inappropriate. Some participants' currencies had no strategic role in the realignment, while the entire financial community has an interest in the outcome. The LDCs were at no time consulted substantively on these negotiations. One of their fears concerned recessionary tendencies stemming from exchange-rate uncertainties and an excessively sharp realignment. On these points, the realignment itself seems

reassuring. At the same time, should the realignment be insufficient to strengthen the U.S. balance of payments, they fear that aid and capital outflows to LDCs may decline further. They are also apprehensive about the increase in the gold price. First, some LDCs have debt in depreciating currencies subject to gold clauses. Second, few hold their reserves primarily in gold or other assets that will benefit from the increase, while they fear that the benefits accruing to holders of gold-guaranteed assets, including Special Drawing Rights (SDRs), will discourage the creation of additional SDRs, slowing the growth of their reserves.

A moderate and brief flow of dollars back to the United States in the first month after realignment brought the spot dollar to a slight premium in relation to more than half the major currencies. By the middle of April 1972, however, the spot dollar had moved to a discount vis-à-vis most major currencies, albeit one well within the newly widened margins for permissible fluctuation of the spot rate. The forward (three-month) dollar in mid-April almost invariably showed a discount in relation to the spot rate of major currencies. Except during a short speculative flurry in late March, intervention by monetary authorities had been minor since the realignment. The speculative flurry occurred before the action of monetary authorities in the United States and elsewhere seemed to reassure dollar holders that interest rates here would move higher relative to those abroad.

The Need for a New System

The August crisis, as already indicated, was the reflection of what many have long perceived to be deep-seated defects of the Bretton Woods system. This view was widely endorsed at the 1971 Annual Meeting of the IMF, as well as subsequently. Reforms are urged regarding the process of balance-of-payments adjustment, the process of liquidity creation, and the resulting structure of the world's liquidity. The adjustment process, it is widely felt, has operated too slowly, especially where disequilibria were so serious that they could be cured only by exchange-rate changes. For this reason, adjustment in recent years has too often come only in the context of severe monetary crises. The process of liquidity creation, it is said, has come to depend on one country's balance-of-payments performance and should be brought under international control. Moreover, the process has contributed to the malfunctioning of the adjustment process, and the structure of international liquidity must be changed if the adjustment process is to function properly.

More specifically, there seems to be fairly wide agreement among

governments on the following points, although (or perhaps because) these points are by no means unambiguous:

1. Need for the par-value system.
2. Need for increased exchange-rate flexibility within that system.
3. Need for measures to deal with movements of liquid capital.
4. Need for the subjection of all countries to the obligations of the adjustment process.
5. Need for giving SDRs an increasingly important role as a component of international liquidity, for a corresponding change in the role of reserve currencies, and for a proper determination of the volume of international liquidity.
6. Need for ensuring a proper degree of convertibility.
7. Need for redefining the role of gold.

There is less agreement on the need for a stronger role for the IMF, which some of the reforms may imply. Points 1 to 4 are relevant to the reform of the adjustment process. Points 5 to 7 refer primarily to the reform of the process of liquidity creation and to liquidity composition.

Work on reform has already started in the Fund. Pending revision of the Articles of Agreement to enact permanent modification of the system, some provisional arrangements have been adopted and others may be needed. The existing provisional arrangements are not, of course, fully consistent with the requirements of the Articles. By suspending certain of the latter (under Article XVI), the Fund could make the provisional arrangements fully legal. But no suspension can exceed 360 days, and the corresponding amendments to the Articles could not be approved within that time span; on technical grounds alone, they are more likely to require up to two years for enactment. It is also likely that agreement on certain basic reforms will be reached, if at all, only with extreme difficulty and delay.

Adjustment

The par-value system. The malfunctioning of the adjustment process, as already mentioned, is blamed in part on the process of liquidity creation, which is thought to relieve certain countries from pressure to contribute to adjustment. But the par-value system itself—the core of Bretton Woods—is blamed for creating unnecessary mechanical difficulties by promoting exchange-rate rigidity without really contributing to exchange-rate stability, the objective of the par-value system. This accusation is false; rigidity was the choice of governments, not a requirement of the system.

The par-value system obliges monetary authorities to maintain market rates within narrow margins of the parity declared to the Fund (in the

present Articles, plus and minus 1 per cent of the parity in terms of gold or U.S. dollars of the weight and fineness existing on July 1, 1944). Various clauses protect the substance of this obligation by prohibiting exchange restrictions and multiple exchange rates except with the permission of the IMF. It is noteworthy, however, that capital movements are exempt from the prohibition; in fact, the underlying philosophy of the Articles is that capital flows that contribute to balance-of-payments disequilibrium are to be prevented, not financed—certainly not by use of IMF credit.

Unlike the classical gold standard, the Bretton Woods system does not require countries to maintain parities at all costs; these may be changed after consultation with and (generally) approval by the IMF, upon showing that the balance of payments is in fundamental disequilibrium. This concept has never been defined. Taken in historical context, however, the possibility of changing parities in fundamental disequilibrium subordinates the objective of exchange stability to the primary objectives of the Fund, namely, the growth of world trade, high employment, and development of the world's productive resources [Article I (ii, iii, iv) of the Articles of Agreement of the IMF]. On the other hand, the limitation to instances of fundamental disequilibrium is deemed to protect other countries against competitive depreciations and other unnecessary changes in exchange rates. By the same token, it is thought to protect necessary parity changes against neutralizing exchange-rate action by other countries.

As already mentioned, most monetary authorities have in one way or another endorsed a return to stable rates, and none has endorsed freely floating rates. This attitude does not mean that major countries bother much about floats of the currencies of LDCs, the repercussions of which on the former are slight, even though they may be pronounced among the LDCs themselves. More generally, there are exceptional circumstances under which few would insist on rate stability: under conditions of very rapid inflation; to achieve gradual transition from considerable misalignment to an equilibrium rate, where LDCs have used controlled rather than free floats with Fund encouragement; to ease a fairly rapid transition from one parity to another, where floats have been used by one developed country; or, finally, where the direction or extent of rate misalignment is too uncertain, as in the two Canadian experiences (1950–62 and after 1970) and the German and Dutch cases in May 1971. That there should be far-reaching loyalty to the par-value system, with the exceptions noted, has seemed surprising to some—even to those who concede that the system itself is not to blame for its many crises, only the way in which it has been operated. Two points seem relevant:

1. Despite its crises, one can hardly claim that the system has served the world badly. *Nobody, of course, can prove that a different system would not have been better*, but the growth since the Second World War in world trade and in the output of both developed and less-developed countries compares favorably with the period of very rapid growth preceding the First World War, as well as with the interwar period. It is nevertheless true that the slow growth of aid flowing to LDCs in the late sixties has often been blamed on the persistence of payments disequilibria among major aid-giving countries.

2. It would probably be impossible to prove that the par-value system is *substantively* better or worse than one that really permitted exchange rates to float freely for countries that did not want to maintain par values. The emphasis is on "permitted," because considerations of political affinity, as well as economics, will understandably suggest to certain groups of countries the convenience of maintaining fixed—even rigid—exchange rates among themselves.

There is, however, a *procedural* consideration that may persuade most countries (even major ones and multi-country monetary unions) to prefer the par-value system to one that permits floats under ordinary circumstances: the alternative of genuinely free floats is simply not available. Parities seem to have at least the advantage that rate changes are subject to international control *ex ante*; without parities, there would be uncontrolled intervention, not market-determined rates, except when market forces happened to behave as the authorities wished. Uncontrolled intervention is rather frightening even if free floats are not.

The propensity of governments to intervene in exchange markets is hardly surprising. Governments interfere with commodity prices like those of steel, which directly affect 3 to 4 per cent of GNP; they are not likely to remain neutral with respect to the exchange rate, which often directly affects as much as 15 to 20 per cent of GNP. Admittedly, the impact of the exchange rate becomes smaller for larger economic units; genuinely free floats might be more realistic among currency blocs. But, in most cases, the exchange rate would still be too important a price for governments to leave alone. One might add that, even if each government were prepared to refrain from intervention provided all others also refrained, one would be no nearer a solution: how would one enforce nonintervention credibly? This is a familiar dilemma.

One might ask whether control *ex ante* over intervention is necessary, for control *ex post* would not require the par-value system. But *ex post* control might leave too much leeway for abuse. Sanctions are hard—probably impossible—to impose effectively in respect of an act as hard to define as an unjustified intervention. The intervention may have done

all its harm before it is identified as unjustified. *Ex ante* control is harder to flout: it may imply condemnation (by the IMF) simultaneously with the announcement of a rate change, and prompt condemnation, besides creating a bad "image," could render the change ineffective by mobilizing the very efficient "Gnomes of Zurich."

One should ask whether *ex ante* control does in fact exist under the par-value system. Though national authorities almost invariably decide upon rate changes without previous formal consultation with the IMF Board, close contact between the IMF staff and the authorities means that national authorities know at any time what the IMF would deem to be an acceptable parity change.

Why is international control over exchange-rate changes so important? A smoothly functioning international economy ideally requires international surveillance over, and coordination of, *all* aspects of economic policy. But if these cannot be enforced to any substantial extent, controlling exchange rates is quite effective. Rates have a more direct impact on a wider range of international transactions than other economic policies, especially domestic policies. Could one argue that the need for surveillance and coordination exists only because of the par-value system? Could they be dispensed with if rates were free to float? This has been shown to be an irrelevant question. Nor, obviously, could one permit floating rates for the benefit of those countries that would float "freely" even if others did not.

Surprise is sometimes expressed that the LDCs (including those with a relatively small foreign sector) should be among the principal defenders of the par-value system, as they have been in IMF discussions. Some of the reasons are explained below and reflect the special fears of those countries regarding the effects upon them of increased exchange-rate flexibility among the major currencies. But the ability of LDCs to live with the par-value system should really be surprising only to those who take a somewhat romantic view of LDCs. Thus, contrary to what is sometimes claimed, not many more LDCs than industrialized countries exhibit a degree of inflation in excess of the world average or otherwise incompatible with the par-value system. In fact, more LDCs than industrialized countries have very low rates of inflation (nor are the stable LDCs growing less quickly than others). From another point of view, the median instability of export receipts for LDCs, while double that for industrialized countries, has not recently been particularly high. In sum, the LDCs in general have the same reasons to prefer—and no more reasons to reject—the par-value system than the industrialized countries.

Flexibility. For several years, a discussion has been going on as to the

possibility of permitting increased market-rate flexibility without undermining the par-value system and its objective of exchange-rate stability. This discussion has been in response to the somewhat subtle accusation that, without necessarily promoting exchange rigidity, the par-value system has discouraged timely exchange-rate changes that would have been justified by a fundamental disequilibrium. This accusation, again, is false: delays in adjustment were the choice of the government concerned rather than a consequence of the system.

Three issues have been in the foreground of the discussion: (1) Are prompt changes in parity compatible with the concept of fundamental disequilibrium? (2) Is it proper and useful to widen slightly the margins around par? (3) Should the IMF be permitted in the future to authorize temporary floats without margins?

1. Are prompt changes in parity—which may mean smaller and more frequent changes than in the past, including reversals of immediately preceding changes—compatible with the concept of fundamental disequilibrium? It has been made abundantly clear that they are and that, indeed, the infrequency of parity changes in the past was a misapplication of the par-value system. In this connection, it should be noted that an orderly revision of the recent realignment would not spell the collapse of attempts to reconstruct the par-value system.

An interesting step was taken in conjunction with the realignment. The Fund decided that, for the time being, countries could declare "central rates" rather than parities. One difference between par values and central rates is that the latter can be expressed in terms of gold, SDRs, or another member's currency, while par values can be expressed only in terms of gold (or dollars of the weight and fineness existing on July 1, 1944): this difference is of little immediate practical importance, though it does suggest a declining role for gold. A more important difference is the fact that changes in central rates do not require prior approval by the IMF, though it must be notified and can challenge them. Immediately after the realignment, thirty countries declared central rates, as distinct from thirty-one that declared or reaffirmed par values. The majority of industrialized countries, moreover, opted for the former. The countries that retained parities were, in the main, those that had not proposed changes in the gold values of their currencies, and all but two were LDCs. Since the U.S. Congress authorized adoption of a depreciated par value by the United States, some LDCs have started to replace the central rates by equivalent par values. The industrialized countries maintaining central rates are expected to follow suit, and the European Economic Community is believed to be

ready to do so as soon as certain technical problems arising out of the common agricultural policy can be solved. The authority to declare central rates will then be canceled.

The institution of central rates is not, however, the answer to the problem of prompt parity changes. Owing to the exemption from prior approval by the Fund, the system based on central rates could lead to disorderly exchange-rate changes more easily than the par-value system, despite the IMF's right to challenge central rates. Thus the latter will be no more than a temporary expedient—like the provision of the Articles allowing countries to change their par values without Fund approval up to 10 per cent in relation to their initial parities, a provision instituted to help bridge the special uncertainties of the postwar period. There is, of course, no reason why prompt parity changes should be less practical than changes in central rates. The Fund is quite capable of giving timely prior approval to requests for changes in par values.

It has sometimes been suggested that small par-value changes (e.g., up to 3 per cent per annum, up to 10 per cent per quinquennium) be similarly exempted from the need for prior approval by, but not prior consultation with, the IMF. It is hard to see, however, what practical advantage such an arrangement could offer, since, in practice, prior approval hardly involves a more cumbersome procedure than prior consultation. Furthermore, the importance of a change is not measured by its percentage alone, but by all the surrounding circumstances; the exemption of small parity changes would thus be most inequitable. It has been suggested that par-value changes might become more prompt if criteria were established for making them and also if the Fund were given power to apply sanctions to countries maintaining inappropriate parities. It would be hard to formulate meaningful criteria and it is doubtful that the international financial community would be prepared to apply sanctions.

2. Is it proper and useful to widen slightly the margins around par? The purpose of this proposed reform is not to affect the trade and service account of the balance of payments, for which a slight widening would generally be insufficient, but to discourage short-term capital flows. It has often been claimed that the danger of these flows prevents prompt parity changes. If parity changes are more timely, and therefore possibly more frequent, the argument runs, speculators are more likely to act on a suspicion of a parity change. As these speculative flows could become self-justifying, authorities should discourage them and the expectations of prompt parity changes that are alleged to produce them. These arguments are not convincing. Since more frequent parity changes are likely to mean smaller parity changes, speculation would be less

profitable than when par-value changes are delayed, infrequent, and large. Thus, the widening of margins seems less helpful to a properly run par-value system than to one run as in the past.

Wider margins are also an instrument to give countries greater autonomy in the use of monetary policy. The appeal of this effect, however, depends very much on the extent to which countries are encouraged to rely on monetary policy rather than fiscal policy in their attempts to control the business cycle. The last word on this has not been written.

While there is some support for slightly wider margins among major developed countries, to most IMF members—particularly LDCs—a slight widening of margins does not appear directly useful. Most of them do not use the margins they are now permitted. By contrast, there would be some special dangers for them. Even slightly wider margins between major currencies might force other countries to choose which of these currencies they would peg to. With only slightly wider margins, this choice would not involve optimum-currency-area considerations. But the need to select a particular currency might be politically embarrassing and could still be economically harmful. Monetary blocs can develop into inward-looking trading blocs, as already mentioned, and the formation of such blocs would be particularly costly to LDCs. Their relative poverty requires them to take every possible advantage of access to world markets, and they may also have an interest in forming customs unions among themselves, including countries belonging to different monetary blocs. If, further, major countries avail themselves of wider margins to place greater reliance on monetary policy in controlling *self-generated* business cycles, they can easily create major debt-management problems for countries pegging to their currencies; greater reliance on monetary policy may lead to wider fluctuations of interest rates. This could create special problems for LDCs having to borrow heavily or to refinance large external debts. Nor would this disadvantage be offset by the fact that, in combatting the effects of *imported* inflations or deflations, the major countries themselves could rely more on movements of exchange rates, which would contribute to interest-rate stability. Slightly wider margins would not allow large enough changes in exchange rates to stabilize the current account of the balance of payments in the face of imported disturbances. Finally, the major countries are likely to be increasingly concerned with self-generated cyclical movements, rather than imported ones, especially if those countries group themselves into economic blocs.

At the time of the realignment, the Fund provisionally authorized margins for spot transactions of up to 2.25 per cent around parities or

central exchange rates in relation to the respective intervention currencies. These margins may cumulate to 4.5 per cent between two nonintervention currencies pegging on the same intervention currency. Thus, swings of up to 9 per cent have become possible in this case, as compared with maximum swings of 4 per cent possible heretofore. Swings of 9 per cent may come close to making nonsense of the par-value regime. The new margins may, however, become less significant if the main European countries succeed in their intention to narrow currency fluctuations among themselves. By the end of 1971, two-thirds of the countries maintaining parities and slightly more than two-thirds of the countries declaring central rates had advised the Fund that they would avail themselves of the wider margins. The countries eschewing the wider margins were exclusively LDCs.

The width of the provisional margins, though very wide, has not been felt to make it necessary to face certain issues that might otherwise have given a great deal of trouble, including the advisability of imposing limits on forward-rate fluctuations. Countries have sometimes deliberately devaluated their forward rates in order to stimulate exports, although they have usually done so only within limits and under circumstances in which a similar parity change would have been justified. Such forward-rate flexibility is obviously less necessary when spot rates can fluctuate more widely. Moreover, no attempt has been made to regulate in any way or limit intervention within the margins. Some countries have expressed sympathy for such limitations, to prevent abuse, but it is hard to see how enforceable rules could be formulated.

3. Should the IMF be permitted in the future to authorize temporary floats without margins? This is a purely procedural point. In exceptional circumstances, as has been seen, the Fund has found it possible to tolerate freely floating rates (where it could not authorize them as part of a multiple-rate system) or even to recommend freely floating rates or rates that were administratively adjustable, often at very short intervals, without the formality of a parity change. The question, therefore, is merely whether such floats should be *legally* available and under what conditions.

One of the arguments for legalization is that mere toleration cannot meet the needs of countries that have great sensitivity for the law, but experience has proved this to be patently untrue. Could one claim that Canada, which instituted its first float before there was anything like a general crisis of the international monetary system, has a particularly deficient sensitivity to law? It has also been claimed that the Fund cannot impose its discipline on surplus countries with floating rates unless

it can legally authorize their floats—or withhold authorization—for it lacks any other sanction. Similarly, it has been claimed that the Fund cannot otherwise discipline deficit countries with floating rates, as they are not affected by restrictions on access to the Fund's resources. These arguments, too, are unconvincing. It is unlikely that countries would fail to obey the expressed opinion of the Fund regarding the manner in which they should float if their floats were merely tolerated but would obey a formal decision as to how they should float if their floats had been formally approved. Furthermore, as long as temporary floats remain exceptions, justified by very special circumstances, they need not subvert the par-value system, even if they are tolerated rather than approved formally. This is true not only of most LDCs and other countries whose currencies have little importance in world trade, but also of important industrialized countries.

Even if all these arguments for legalizing temporary floats were valid, a further problem might arise. There might be a tendency to legalize (or approve legally) only floats that seemed *ex ante* to be very limited in time though they might turn out to be lengthy, while floats that appeared to be lengthy *ex ante* would not be legalized. This tendency would stem from the fear that legalization of a wide range of floats would lead to dangerous abuse; the IMF might settle on *expected* duration in order to narrow the range. It should be noted, first, that this argument contradicts one mentioned earlier in support of legalizing the narrower range of floats—that legalization itself prevents abuse. But there is an even more important point. The LDCs happen to be the principal users of those rare floats that appear *ex ante* to be lengthy. If, tomorrow, a legal distinction emerged between floats that are on a par today in respect of legality, the LDCs might find themselves exposed to more onerous conditions than they are today, and to more onerous conditions than the industrialized countries.

To summarize, the most important recent development in the conception of the par-value system is the emphasis on the compatibility of prompt (possibly frequent and small) par-value changes. But other changes, in mechanics, pose problems. "Central rates" or an equivalent form, subject to challenge but not to prior approval by the Fund, presents dangers to the maintenance of orderly exchange conditions. A slight widening of margins has doubtful advantages and some disadvantages, especially to smaller countries and to LDCs. If the widening of margins is slight, these disadvantages will be tolerable, but only experience can tell whether the experiment recently started should be continued. The legalization of other departures from the par-value system, even in excep-

tional circumstances, is substantively unnecesary, since Fund acquiescence in such practices may be adequate. If, however, legalization became necessary, it would have to be general to avoid grave inequities.

No support was expressed in international discussions for any substantial widening of margins. This would, in practice, be indistinguishable from abandonment of the par-value system, particularly as enforceable intervention rules would be hard to formulate. Nor has there been thus far any sympathy in official circles for the "crawling peg" or "crawling band," whether in "discretionary" form or in "automatic" or "formula" form. This, again, should not be surprising. Since it seems impracticable to formulate rules for the use of discretion, "discretionary" crawls would be uncomfortably independent of *ex ante* control; and it may be impossible in practice to distinguish "formula" from "discretionary" crawls, since the independent variables entering the formula are susceptible of manipulation.

Other measures. Recent experience with short-term capital flows has increased interest in measures to stem them (in addition to the widening of margins). The Bretton Woods prescription for the problem, as already mentioned, is quantitative capital controls, and some countries have expressed sympathy for them. Other instruments developed recently to inhibit short-term capital flows include reserve requirements against foreign borrowing, not only by banks but also by enterprises, and special taxes (which need not be multiple rates). As for flows that cannot be stemmed but are not due to fundamental disequilibria, large means of financing them are already available and additional mechanisms can easily be created.

An important way to minimize or avoid short-term capital flows prompted by interest-rate differentials is to coordinate monetary policies and place greater emphasis on fiscal policy to deal with the business cycle in industrialized countries. Recently, despite the obstinacy of the recession in the United States and because of the fear of deepening recession in Europe as a result of the realignment, monetary policies have at least not been in flagrant conflict, although interest-rate policies have not yet been sufficiently aligned to stimulate a reflow of privately held dollars to the United States. It would be unrealistic, however, to expect a rapid shift toward reliance on fiscal policies and an early coordination of monetary policies. Both are problems which, in the context of an essentially stable rate system, will have to be faced, but the institutional and political obstacles loom large. Certain European countries would like the United States also to limit outflows of direct investment capital. The purpose here, of course, is not only to relieve pressure on the current account for balance-of-payments adjustment. In all these cases, the LDCs

would prefer inflow rather than outflow controls, because the latter would have to be global in order to prevent outflows to countries not objecting to inflows from being transferred to countries that do object. Such worldwide outflow controls could easily result in undesirable restrictions on outflows to LDCs.

The "burden" and its distribution. It has often been claimed that the Bretton Woods system lacks incentives to promote prompt adjustment by surplus countries. Similarly, as already mentioned, it is said to put insufficient pressure on certain deficit countries, namely, reserve centers and others with privileged access to balance-of-payments finance. The "burden" of adjustment, in other words, is said to be unfairly and inefficiently distributed.

The concept of burden sharing implicit here is political—the need to take explicit action. From this point of view, a surplus country is often, but not always, better off than a deficit country: it can generally afford to wait until the deficit country is forced by a lack of finance to take explicit action (unless the deficit country is a reserve center). This is unpleasant for the deficit country. It may also make for an unnecessary volume of decision making in the international financial system, raising the total of political pain in the world and leading, also unnecessarily, to less prompt adjustment than would occur if there were greater incentives for explicit action by surplus countries and by privileged deficit countries. It may not necessarily be most convenient from the point of view of the world that *all* countries in disequilibrium be forced to take explicit action. If, for example, a surplus is concentrated and its counterpart is widely diffused, so that there are relatively few countries in equilibrium, the need for explicit action is minimized if the deficit countries do not adjust; only the few surplus countries and the few in equilibrium then have to act.

By contrast with the political "burden" of taking initiatives, which some countries can often escape, *no country can escape undergoing an economic restructuring* whenever balance-of-payments adjustment requires a change in real demand or supply. This *process* of adjustment will generally involve transitional unemployment, and there will be additional unemployment and inflationary distortions whenever domestic prices and wages are not perfectly flexible at least in one direction. That this process *must* be harder on deficit than surplus countries is a stubborn illusion, applying only on the combined assumptions that adjustment must be brought about by internal means *and* that all countries prefer inflation to unemployment. A deficit country (that does not wish to leave the initiative to the surplus countries) can adjust by deflating, and creating additional unemployment, or by devaluating, and

risking inflation. But a surplus country (that does not wish to leave the initiative to the deficit country) has no better option; it can choose between inflation and revaluation, which risks creating additional unemployment. Finally, insofar as unemployment is considered a greater evil than inflation, the deficit country might even be considered better off; it can escape unemployment by one irreversible stroke—devaluation. Because exchange-rate changes can be justified only by fundamental disequilibrium, whichever country in fundamental disequilibrium acts first on its exchange rate is protected against neutralizing exchange-rate action by others. If the surplus country prefers inflation to the risk of recession consequent upon revaluation (or devaluation by the deficit country), it cannot ensure its choice by an irreversible stroke but may have to make repeated attempts—as by offering to finance the deficit country—which the latter may not accept. The only irreversible stroke open to the surplus country is revaluation, and that may mean opting for deflation and unemployment. From the point of view of third countries, devaluation by deficit countries may have a different effect than appreciation by surplus countries on the purchasing power of reserve assets, and the distribution between deficit and surplus countries of internal measures designed to reestablish balance-of-payments equilibrium may also affect third countries differently.

It may be convenient at this point to exorcise a confusion concerning the concept of economic burden of adjustment. It has become fashionable to speak of the permanent or continuing "cost of adjustment" or "cost of accomplished adjustment," as distinct from the burden of the adjustment *process*. The former concepts have been variously defined (see Cohen, 1966, p. 5, and Krause, 1971, p. 27) as (1) the reduction in real absorption by the deficit country and (2) the reduction in the deficit country's share in the joint real absorption of deficit and surplus country. Neither (1) nor (2) necessarily characterizes accomplished adjustment. The first may not occur if adjustment of the current account is accompanied by an increase in employment and output of the deficit country. The second will not occur if adjustment takes place through the capital account rather than the current account (e.g., a change in net long-term capital flows). Finally, it is meaningless to speak of a continuing burden or burden of accomplished adjustment when, in the long run, some sort of adjustment is unavoidable; to the extent there is no alternative, there is no cost or burden.

To return to the inequities of the Bretton Woods system regarding the division of the *political* burden of adjustment, what can be done to bring pressure to bear on a surplus country to take internal or exchange-

rate action to contribute to the adjustment process? The Fund disposes of the right to declare a currency scarce, and such a declaration authorizes members to discriminate against the scarce-currency country in exchange transactions. This power has never been used and is considered too disruptive of international economic cooperation to use, even if it were effective. But the Article dealing with scarce currencies could be reformed to make it usable. The Fund could be empowered to *require* that a surplus country lend its currency to the Fund at long term; the Fund can now suggest that it lend but not demand it. Remuneration would have to be low, to offset the gold (or SDR) guarantee implicit in loans to the Fund. (A limited compulsory lending obligation was part of the Canadian proposals that preceded Bretton Woods.) Keynes's old idea of charging the surplus country a penal interest rate on its reserve accruals is also interesting but may meet particular tactical difficulties at this time. Neither reform, moreover, would place as much pressure on a surplus country as is experienced by a deficit country that lacks balance-of-payments finance. It might also be mentioned in this connection that the Fund has the power (in general and under the scarce-currency clause) to make and publish reports that—apart from exerting "moral suasion"—might help to compel a country, whether in surplus or in deficit, to initiate action by evoking action by speculators. This power has never been used, and the international financial community might not want the Fund to use it.

The different degrees of pressure to adjust exerted by the present system on ordinary deficit countries, as distinguished from privileged deficit countries, stem in part from the process of liquidity creation. But it cannot be too strongly stressed that they do not stem from it exclusively. Thus, as long as the United States remains the world's major economy, it will be able to find means to finance its deficits that are not open to other countries—even if the United States ceases to be a reserve center. Differences in the economic weight of other deficit countries will create similar discrepancies. It is therefore naïve to believe that anything even remotely approaching an equitable distribution of the political burden of adjustment can ever be established among the deficit countries themselves. Moreover, even if the special access to balance-of-payments finance does not take the form of creating reserve currency for other countries to hold, the accumulation by major countries of deficits they may be unable to repay could still induce very grave monetary crises. In the case of major countries, there is no substitute for self-discipline. But this is no reason to abstain from attempts to reform the system in order to promote greater equity.

Liquidity

The development of the system. As has often been emphasized, the process of liquidity creation that has emerged since 1945 was not a consequence of the Bretton Woods system as originally envisaged. The original conception was that countries would hold international reserves in gold. Their ability to ride out temporary balance-of-payments deficits was to be bolstered by access to the Fund's resources, but this access was conditional. In accordance with the Fund's rules, reserve currencies would play a role subordinate to gold and IMF credit, even though national currencies would be used for market intervention rather than gold, as before 1914. Convertibility into gold was to be a substitute for market intervention.

This simple view of international liquidity was gradually overtaken by events. The growth in the volume of world trade and the postwar inflation created additional liquidity needs. These were met to a small extent by the accrual to monetary reserves of new gold production. Eventually, however, the fixed gold price prevented any further accruals and even led to gold losses from global monetary reserves. These were stopped in 1968 by the agreement that central banks would not supply the private market with gold from reserves and would also refrain from making purchases in that market. At the moment, only small amounts of gold flow into official reserves: the IMF purchases gold from South Africa under specified circumstances and resells it to member countries in proportion to their net creditor positions in the Fund.

Drawings on the Fund have added to reserves by creating reserve positions in the Fund. Increases in Fund quotas have likewise increased the volume of conditional international liquidity, while bilateral credits have increased liquidity among a small group of countries. But the major increase in unconditional liquidity has come from an increase in dollar balances held by monetary authorities. (Until very recently, changes in other reserve currency holdings made no net contribution to liquidity.) These dollar accruals, however, together with the gradual redistribution of the very large gold stock held initially by the United States, eroded the gold "cover" of foreign-held dollar liabilities. This created the possibility of monetary disturbances as the world came to feel that it held too many dollars. This has often been called the "confidence problem." It might be added that such a problem need not have arisen if dollar liabilities had been matched by short-term rather than long-term U.S. assets abroad; on one definition of the balance of payments, there would then, of course, have been no deficit.

To create sufficient additional liquidity of an unconditional nature,

without having to rely on increased dollar liabilities, the SDR facility, or scheme, was developed. SDRs are allocated to Fund members participating in the Special Drawing Account on the basis of Fund quotas, without counterpart. Countries pay modest charges on the amounts allocated and receive a modest interest rate on the amounts held. While SDRs were primarily regarded as a gold substitute, it must be realized that, in the last analysis, dollar reserves were also a gold substitute and, in this limited sense, SDRs are a dollar substitute as well, even though they show certain weaknesses in their present form compared with the dollar, as well as with gold.

It might be said that, as long as the United States was supplying the world with dollars by running deficits, there was no *need* for SDRs—except to the extent that the U.S. deficits themselves reflected the world's need for liquidity. Yet even if U.S. dollar liabilities to official holders were still rising, SDR allocations could be helpful. By endowing surplus countries with additional liquidity, they might reduce marginally the incentive to earn liquidity through balance-of-payments surpluses. In this way, the surplus countries' willingness to contribute to the adjustment process might be marginally increased. By the same token, pressure on the United States to limit its deficits might be marginally increased, if the availability of an alternative source of liquidity made the world less willing to accept dollars.

"Discipline" via "convertibility." It is widely believed that discipline over reserve centers can and should be established by arresting the growth of foreign official holdings of national currencies, or by limiting it to intervention needs. Attention has naturally focused on the dollar, but it should be clear that other currencies may assume (or reassume) the character of reserve assets. Furthermore, "discipline" is required not only over reserve centers but also over other privileged deficit countries, and over surplus countries. Finally, it should also be remembered that "phasing out" the dollar as a reserve currency, as it is sometimes called, cannot do much to establish "discipline" over the world's major economy. But there is no reason to make the running of deficits too easy for any country.

How, then, should the dollar be "phased out"—and other currencies be prevented from "phasing in"? It has been suggested that the United States (and reserve centers generally) regularly redeem all future currency balances accruing to official holders—not merely stand ready to do so, as in the past—using for that purpose whatever reserve assets it may command or the currency of the country presenting the dollars (which it could borrow or purchase from the IMF). In this way, no country could run deficits beyond those it could finance with reserve

assets or borrowings (save to the extent that the world needed larger balances of an intervention currency—and even this should not require reserve centers to run deficits for some years).

Before convertibility of this kind can be effectively established, two major problems must be solved. First, some means must be found to deal with the so-called "overhang" of currency balances in official hands. It must not be presented for conversion and thereby absorb the issuers' reserve assets (which should remain available to meet future deficits). Nor must its existence and use altogether prevent the issuers from adding to their reserve assets if they run surpluses. Further, it is necessary to protect the realignment of exchange rates from attempts by one central bank to unload its excess currency holdings on another (not the issuer). More generally, switches of existing currency holdings into and out of other reserve assets should be prevented, as they could lead to haphazard fluctuations in the volume of reserve assets. (We speak here only about balances held by official holders. It is analytically convenient to treat the movements into the hands of central banks of balances privately held abroad as an ordinary capital outflow from the reserve center, which may bring about an overall balance-of-payments deficit.)

Second, it will be necessary to make sure that the reserve assets of the reserve centers are adequate to meet the temporary deficits they may suffer in the future. The discussion below refers generally to dollars and the United States but is, of course, applicable to other reserve or intervention currencies and to the respective issuers, insofar as they confront the same problems as the United States.

Regarding the first major problem, the "overhang," a long-run solution with apparently great appeal is the replacement with SDRs of existing official holdings of dollars in excess of each country's precise need for working balances. The Fund would be empowered to make a special issue of SDRs in exchange for dollars and other reserve currencies. [Central banks, to illustrate the problem of the "overhang," are currently sometimes reluctant even to allow their currencies to be used for repurchases from the Fund, as this involves them in the acquisition of additional dollars from the repurchasing country. It has been necessary to arrange for simultaneous drawings of these currencies from the Fund, so that the net dollar holdings of the issuers of currencies used for repurchases do not rise on account of Fund operations. To avoid the need for matching drawings and repurchases, which could limit the Fund's usefulness to its members, some countries would like the United States (and other issuers of reserve currency) to begin *now* to convert into gold or SDRs those dollars that accrue to other central banks by reason of the use of their currencies in Fund repurchases and those held

by countries with insufficient gold or SDRs to make payments to the Fund.] If SDRs were issued in place of dollars, there would be no excess dollars to present to the United States for redemption unless it was running deficits. If the United States ran surpluses, it would build up its gross reserves rather than reduce its liabilities; any dollars held in working balances that were used to pay off a United States surplus would have to be repurchased by sale to the United States of SDRs. This arrangement would prevent attempts by central banks to unload on each other what they may consider excess dollar balances under present conditions of inconvertibility, thereby reducing the potential for disruption of the realigned rate structure, which may be perfectly viable from the longer-run point of view. Finally, the volume of international liquidity could not decline as a result of switches out of dollars, nor could it increase by switches into dollars.

All these effects, except the very last, would follow automatically, without need for international surveillance or guidance. The last would require that the Fund be empowered to direct the United States to redeem its currency from another country against SDRs even if the latter did not wish to give up its dollars. The system would have an additional advantage. If reserves were not held in national currencies, it would be easier for the respective issuers to change exchange rates, because changes would then have no effect on the relative purchasing power of reserve assets. The replacement of dollars with SDRs would, however, present very difficult problems.

Should the replacement be voluntary or compulsory? The difference, to be sure, may be smaller than it appears at first. Compulsory replacement could not, by itself, guarantee to extinguish dollar holdings not strictly needed as working balances, as there is no adequate definition of the latter and there are means of disguising the volume of official holdings. In effect, then, the replacement would always be voluntary to some degree. But this implies that any once-over replacement with SDRs would leave dollar holdings that might later be deemed excessive by monetary authorities. Hence, the replacement of dollars with SDRs would not positively avoid any of the difficulties mentioned above as constituting the first major problem, though it would certainly greatly reduce them.

It would be possible to avoid these difficulties, even if countries held more than working balances, but only by relying on comprehensive and cumbersome guidance regarding central banks' international transactions. Thus the United States would convert only at the order of the Fund to avoid having to redeem dollars held in excess of working-balance needs. Further, to make sure that the United States earned

reserve assets when it ran surpluses, the Fund would have to be able to direct countries to redeem dollars from the United States against delivery of SDRs, or would have to be able to issue SDRs to the United States whenever total official holdings of dollars were declining. To prevent the offloading of reserve-currency holdings by one central bank on another, each country would have to agree not to use its holdings of reserve currencies except to purchase its own currency from the market where necessary to prevent the rate from falling below its lower intervention point. In other words, central banks would have to agree not to attempt to diversify their holdings of national currencies. In brief, the use of dollars would have to be regulated by balance-of-payments need, like SDRs, and the Fund might have to acquire new powers of direction in this connection.

It is also clear that, if the Fund were given sufficient powers, the underlying difficulties that constitute the first major problem could be avoided even without replacing existing dollar holdings with SDRs. This means that there would be little practical value in either a voluntary or a compulsory replacement that did not serve to reduce working balances to very low levels. A reduction to such levels, however, would be valuable, precisely because the system could then be run without undue risk in the absence of detailed guidance. Guidance would be required only to prevent an increase in official dollar holdings (not warranted by need for working balances). There is a vicious or virtuous circle here. The more far-reaching the replacement, the more could use of SDRs be freed from shackles that constitute one, though only one, factor discouraging the replacement.

Another problem to be solved in order to effect replacement concerns the acceptance obligation for SDRs. If the replacement were voluntary, would all participants in the SDR scheme have their acceptance obligations increased? Obviously, those who had not participated in voluntary replacement might object to such an increase; this could reduce the acceptability of SDRs, making voluntary replacement less attractive.

More generally, to make voluntary replacement a success—or compulsory replacement acceptable—the attractiveness of SDRs would have to be increased relative to reserve currencies. At present, SDRs are not overwhelmingly attractive. They are guaranteed in gold, but this feature may become less attractive as the world gets used to SDRs. It is more important over the long run to guarantee the stable purchasing power of SDRs in relation to currencies in general. The 1971 realignment, by devaluing the dollar in terms of SDRs (and gold), went some way toward reassuring SDR holders in this respect. Another way of increasing the attractions of SDRs would be to raise the interest paid

to holders. Presumably, interest earned by SDRs distributed in return for reserve-currency holdings would be paid by the reserve center, not from charges on allocations as they are now. But increased earnings on *allocated* SDRs would have to be paid from increased charges on them. Furthermore, increased remuneration would have to be offered on reserve positions in the Fund, and these would have to be paid from increased Fund charges on drawings. The rate of remuneration would have to be raised to deter countries whose currencies would be drawn from frustrating the use of the Fund's resources. Deficit countries would be reluctant to bear these added burdens, yet surplus countries might oppose a reduction in allocations of SDRs (in order to pay higher interest on them without raising charges on their use). To use some of the interest furnished by the issuers of reserve currencies to pay interest on allocated SDRs and reserve positions in the Fund would reduce the attractions of replacing dollars with SDRs. The same effect would be achieved by using part of the interest of dollar balances taken over by the IMF for amortization of these balances. On the other hand, to insist on amortization on the basis of current surpluses of the United States might be excessively deflationary.

Other current characteristics of SDRs may be equally difficult to correct. Some countries, especially LDCs, have deposited dollar reserves with commercial banks against which their own commercial banks in the United States obtain credit facilities. They risk the loss of these credit lines if they withdraw their dollar reserves to exchange them for SDRs. This problem could be resolved only by changing the provisions of the Articles to permit the deposit of SDRs with commercial banks, and this would be a far-reaching, though by no means impossible, change in the system. A less serious problem posed by the replacement of reserve currencies by SDRs—the withdrawal of central-bank deposits from commercial banks in the issuing country and sales of securities in its markets —could be resolved with relative ease by appropriate central-bank and treasury operations.

Doubts might arise as to whether, in the case of international disturbances, the United States would be as willing to permit even a friendly government to use dollar balances newly acquired with SDRs than dollar balances already held, or whether, in those circumstances, it would fulfill all its acceptance obligations. Such doubts can have no basis in fact, but they might nevertheless exist. Traditionally, countries hold their "war chests" only in gold, but they may include dollars, and these may be preferred to SDRs for this particular purpose.

An amendment to permit the replacement of reserve-currency holdings with SDRs would take time to enact—considerable time. In the

meantime, if convertibility of dollars currently accruing (and of other possible intervention currencies) is to be enforced, other means of dealing with the dollar overhang would have to be relied upon. It has been shown above that this would be possible if the Fund were given the necessary additional powers. It would take too long to confer these powers by amending the Articles, but a Fund decision, based on the members' obligation to cooperate with the Fund to preserve orderly exchange arrangements [Article IV, Section (4)c] could be adopted. Alternatively, an agreement might be negotiated among the major central banks, but this would hardly be quicker and would have the great disadvantage of excluding the bulk of Fund members from participation in and responsibility for an important contribution to the working of the international monetary system.

It may also be appropriate for an issuer of a reserve currency to guarantee official holders an attractive interest rate on their balances of its currency, pending the replacement of reserve currencies by SDRs. Such a rate would not necessarily follow market rates downward. Another incentive to retain such balances would be a maintenance-of-value guarantee, preferably in terms of the issuer's own price level, rather than exchange rates, which would discourage parity changes. The problem to be solved is different from—though not easier than—that of the sterling balances, which was met by the Basle agreements. The latter were designed also to ensure the convertibility of a secondary reserve currency into the primary reserve currency; this is not practicable in the case of the dollar.

The additional attractions suggested above, which might be offered provisionally to holders of dollar balances and which constitute a sort of substitute for convertibility of these balances, pose obvious difficulties for the United States and might still be insufficient to satisfy the holders.

Some central banks may, in any case, want additional guarantees against the possibility of being the main recipient of dollars from countries other than the United States. They may therefore require that every central bank (other than those of the issuers of reserve currency) repurchase some or all of the reserve currencies they lose with gold, SDRs, or reserve positions in the Fund. The present arrangements governing SDR transactions and IMF drawings and repurchases might be used to direct SDRs and Fund positions to the appropriate surplus countries.

A completely satisfactory system for dealing with the overhang of dollars cannot be quickly established. Moreover, the more issuers of reserve currencies are persuaded to help by increasing the attractiveness of their currencies to official holders, even for the interim period, the

less attractive an eventual replacement with SDRs becomes. On the other hand, the smaller the increase in attractiveness of reserve currencies in the interim period, the greater the threat to the realignment of exchange rates, despite a grant of new powers to the Fund. None of these problems requires for its solution tremendous sacrifices by any particular country, and the overhang *could* disappear quickly, by reflows of dollars. The stakes, however, are high: the breakdown of the realignment in the short run (which may, of course, be unimportant to some countries) and the retreat from international cooperation that would follow in the long run from the breakdown (which cannot be unimportant to any country). All this would occur because of a situation that is hardly likely to endure, since dollar glut is no more a structural problem than dollar shortage proved to be.

Once existing dollar balances have somehow been dealt with, it becomes possible to provide for regular conversion of intervention currencies currently accruing to surplus countries, but only if, by that time, the second major problem mentioned earlier has been resolved. The United States must have accumulated a volume of reserve assets commensurate with likely future deficits. In the short run, the United States can certainly not be sure of having the necessary surpluses, since the full effects of the December 1971 realignment, together with other measures to be taken to bolster the U.S. balance of payments, will not be felt in less than one or two years. Some means must therefore be found to finance prospective U.S. deficits and for the United States to accumulate reserve assets.

The simplest way to deal with this problem would be a stabilization loan to the United States. This expedient sounds peculiar when applied to the world's wealthiest country, but it has often been tried in other countries. Such a loan could, in theory, be made large enough to mop up both existing excess holdings of dollars (over and above what each holder wanted to retain as a working balance) and to permit the complete redemption of future accruals. But such a loan would have to be very large indeed. Moreover, it would reduce the liquidity of the country granting it more than if its dollars were converted into SDRs—more even than an agreement to use its dollars only to meet a balance-of-payments need. A stabilization loan designed merely to permit the conversion of future accruals, not to mop up existing holdings, might be more acceptable. It has been suggested that a stabilization loan of this kind could in fact be quite limited, since the United States has at its disposal not only over $13 billion of reserve assets but a Fund quota of over $7 billion.

Another way of dealing with this problem would be a partial redemp-

tion of dollar balances. Using the old European Payments Union as precedent, it would be possible to require that the proportion of dollars redeemed increase over time. This solution, however, would require cumbersome periodic negotiations, since the size of the deficits during the readjustment period can hardly be foreseen. To fix a maximum redemption per annum for the period as a whole, whether in absolute terms or as a percentage of U.S. reserve assets, would remove any incentive for the United States to limit its deficits, though it would have the virtue of encouraging other countries to limit their surpluses.

The disadvantage of replacing convertibility plus immediate conversion with the substitutes mentioned earlier (attractive interest rates and a purchasing-power guarantee) are particularly obvious in this case; they would not only involve less "discipline" but sacrifice international control over liquidity as well.

One should be clear, however, that as long as a single national currency (or very few) is used for intervention, the existence of working balances unregulated as to size is a potential source of instability. To make absolutely sure that the system could run without international surveillance and guidance, thereby maximizing the attractiveness of SDRs as reserves, no national currency could be used for intervention (though it should be stressed again that, even under those circumstances, monetary crises could occur if countries overborrowed). Under the classical gold bullion standard, gold was used as the intervention medium. Those having payments to make abroad could buy it from their central bank when the market rate for the domestic currency threatened to exceed the intervention point (instead of being able to buy only intervention currency). It would not be impossible to use SDRs in a manner analogous to gold. It would be necessary, for this purpose, to amend the Articles of Agreement to permit private parties to hold SDRs; at present this is prohibited. Central banks could then buy and sell SDRs under the same conditions as they used to buy and sell gold to private parties. One could draw quite narrowly the circle of private parties entitled to deal in SDRs (e.g., private financial institutions only). These parties would buy SDRs from their own central bank when they could not buy needed foreign currency within the intervention limits. Moreover, they could be made subject to a maximum holding limit, so that they would have to pass on the SDRs quickly to the issuer of the currency desired. It would certainly be advisable not to *bar* such a possibility in any reform of the Articles. But, for the time being, and probably for a long time ahead, the idea looks too radical to be acceptable.

There are, however, other ways to avoid the need for a principal intervention currency. The central bank in each country, including the

United States, could stand ready to buy or sell any currency that traders and others wished to acquire or dispose of. It would obtain the currencies it needed, if intervening on the selling side, from the issuing central bank against reserve assets and, if intervening on the buying side, would sell the currencies acquired to the respective central bank for reserve assets. Of course, if world trade continued to be invoiced in a few currencies only, such a system could require complicated rules to avoid the reappearance of a principal intervention currency. Something very similar to such a multi-currency intervention system may be needed if the spread of controls over private capital movements interferes with private arbitrage so that consistent cross-rates have to be maintained by central banks themselves.

In the present context, the advantage claimed for multi-currency intervention is that it discourages the holding of reserves in any particular national currency, because of the absence of a principal intervention currency. If the par-value system were abandoned but central banks continued to intervene, another aspect of the multi-currency intervention system would become important: all countries would be able to change their exchange rates by market intervention, something the issuer of the principal intervention currency cannot do. The main disadvantage of the multi-currency intervention system is that it requires rules to prevent inconsistent intervention, and such rules may be hard to enforce. One simple rule would be to permit intervention only if the rate for any currency in terms of any other one is at its floor or ceiling. If intra-marginal intervention were to be permitted, however, the rules would have to be a great deal more complicated. Another disadvantage of the multi-currency intervention system is that it could hardly become a general system. Some countries might wish to continue to intervene in one currency only. Even if they did not, other countries might refuse to intervene in the currencies of the former countries or might deny them the swap facilities of the central bank that are necessary to make the system work smoothly and cheaply. This problem could be of concern to LDCs.

Discipline over privileged deficit countries. It would also be desirable to eliminate the privileged position of some countries that are not reserve centers but are able to create bilateral balance-of-payments credit for each other, without any international surveillance. Before August 1971, the bilateral credit lines of the Group of Ten were about as large as their IMF quotas and equal to one-fifth of their reserves.

One could hardly prohibit these credits, but one could make their use less attractive and, above all, their existence less necessary by offering an alternative source of credit more readily susceptible of surveil-

lance. The simplest but not the easiest way to offer countries an alternative would be a large increase in Fund quotas. Another possibility would be a network of two-way stand-by arrangements. Countries would enter into stand-by arrangements with the IMF of the ordinary kind (i.e., which entitle them to draw without further negotiation). At the same time, the Fund would enter into a new kind of stand-by arrangement with its members by which it would be assured of the ability to borrow from them without further negotiation.

Is there a gold problem? In the system that could eventually emerge, liquidity would consist of small amounts of national currencies held for intervention purposes, SDRs, and probably gold. SDRs would be issued to replace national currencies, but would also be issued or retired as necessary to meet needs for increasing or declining liquidity. It would, of course, be possible in the process of reform to establish a so-called "organic" link with development aid. Some LDCs would prefer a change in the allocation formula in their favor. In addition to SDRs, drawing rights on the IMF should continue to supply conditional liquidity, and changes in quotas should be made periodically, as necessary, to adjust the supply of conditional liquidity.

A system in which national currencies, as well as SDRs and gold, function as reserves and in which the former are freely convertible into the latter, is exposed to sudden switches that may lead to undesired variations in the volume of international liquidity and, depending upon the volume of reserve assets at the disposal of the issuer of reserve currency, to monetary crises. We have already described ways of using and modifying SDRs to deal with these problems. The continued existence of gold as a reserve asset does not present any additional problem.

If national currencies disappear from reserves or, failing that, the private gold market remains rigorously separated from the official "market," sales to or purchases from the private market cannot lead to fluctuations in total international liquidity. Furthermore, for as long as gold and SDRs continue to be mutually inconvertible, their coexistence cannot induce a monetary crisis. Finally, for as long as gold maintains its fixed constitutional link with SDRs, it serves merely as an SDR imprinted on metal rather than one entered in the books of the Fund. The world could therefore continue to live very comfortably with the bulk of its international reserve assets in gold and SDRs, which they would sell to or buy from the issuers of intervention currency against excess holdings of such currency. The only change that would become necessary, compared with the present system, would be to permit an issuer of intervention currency to convert that currency into gold or

SDRs at its option, unless it wanted to redeem its currency in the converting country's own currency or a third mutually acceptable currency.

Unfortunately, one of the strategic assumptions above may not be valid indefinitely. The so-called "gold accord" of March 1968 may not continue to hold. In consequence, it may be necessary to make sure that the gold problem remains innocuous. This could be accomplished, in theory, by extending the consolidation or replacement of reserve assets by SDRs not only to national currencies but also to gold. Consolidation could be achieved by an exchange of gold for a special issue of SDRs. Gold turned in to the Fund in this way would be held in the Special Drawing Account. Once consolidation had been achieved, the system could still break down if countries decided to unwind the SDR facility, but the breakdown would be more difficult, as explicit decision by a large number of countries would be required.

An issue of SDRs against gold would create some problems not encountered in exchanging dollars for SDRs. The same interest rate would have to be paid on SDRs issued against gold as on those issued against dollars, yet there would be no comparable source for those payments (an issuer of reserve currency). It would be necessary, then, either to create a differential between (1) the interest paid on SDRs and (2) the SDR charge on net cumulative allocations and the service charge to the issuer of reserve currency replaced by SDRs, or to reduce allocations in order to use the issue of SDRs to defray the interest to be paid on SDRs exchanged against gold. The first solution would be unfair to users, the second to those countries holding a relatively small part of their reserves in gold—which includes many industrial countries and most LDCs. If the gold received by the IMF were sold to the private market, the currencies received in this fashion could be invested to earn the interest that must be paid on SDRs issued for gold and, perhaps, part of the interest to be paid on SDRs allocated. Alternatively, the proceeds from gold sales to private markets could be used to finance loans to LDCs. No doubt, however, the international financial community would wish to restrict such operations carefully. In fact, some investment of currencies received in return for gold sales might be necessary in order to render these sales neutral from the monetary point of view.

It is popular these days to discuss the "demonetization" of gold. For all practical purposes, the only way to demonetize gold is for the entire world's monetary gold stock to be acquired by the IMF and exchanged against SDRs (or reserve positions in the Fund); otherwise, gold-holding monetary authorities would be deprived of their reserves or might

have to sell them off in the private market against currencies—which could lead to disorderly exchange arrangements.

A few words might be said here on the highly ingenious concept of a reserve settlement account (RSA). Such an account would be an alternative to conversion into SDRs for consolidating reserve assets and reserve currencies. By amendment of the Articles of Agreement, the Fund (or, by agreement, some other international institution) could establish an account into which countries would pay all their reserve assets—national currencies, gold, and SDRs—except (presumably) working balances of the intervention currency. SDR allocations would continue to be made, but would at once be turned over to the RSA. Claims on the RSA would be used in settlement just like SDRs. If national currencies continued to coexist with claims on the RSA in countries' international reserves, the problems encountered would be exactly the same as those described earlier with reference to the absorption of national currencies by an issue of SDRs. It is claimed by some, nevertheless, that the RSA would be superior to an exchange of gold and national currencies for SDRs. It has previously been noted that there might, indeed, be reluctance to make such an exchange, but it is hard to see why this reluctance should be diminished by an exchange into RSA claims rather than into SDRs. Admittedly, countries would retain title through the RSA to the underlying reserve assets they had contributed, particularly to gold, but this is not a substantial advantage, as these assets could be realized only by bringing the scheme to an end. It has been suggested that reserve assets need not be physically transferred, but merely credited to the owner in the RSA account. The same, however, would in principle be possible in a consolidation with SDRs. In the last analysis, any form of consolidation of reserve assets is no more than a rule on the use of reserve assets; as already mentioned, consolidation could be replaced by such a rule (without the need for an amendment of the Articles), if one is prepared to live with the guidance and policing that its enforcement requires.

There is, in addition, one decisive objection to a Reserve Settlement Account. It would set up a new international currency, in the form of claims on the RSA. There might be a temptation to set up the Account outside the Fund, among a limited group of countries. These countries might then feel that claims on the RSA could be increased without increases in SDRs. Nonmembers of the RSA—small countries and, in particular, LDCs—would most probably suffer.

How, further, would the IMF operate in the new situation? If gold were maintained as a reserve asset and a fixed-value relationship main-

tained between it and SDRs, there would be no need for excluding gold from use in Fund transactions. In order to prepare for a system without gold, one might want to provide in any amendment that Fund operations be based on the maintenance of the SDR value of Fund assets (rather than the gold value). Similarly, it would be desirable to permit the use of SDRs whenever it is now permissible to use gold. This would also require changes in the Articles. To give an example, it should be permissible to use SDRs in making the 25 per cent subscription to quotas that today must be made in gold. Such a provision would enter into conflict with the objective of "phasing out" gold from the international monetary system by concentrating it in the hands of the IMF. But that objective has to be faced up to directly, not via gold subscriptions.

The Common Denominator

What should be the common denominator, or numeraire, for the international monetary system? So far, this function has been performed by gold (or dollars of the weight and fineness existing on July 1, 1944). But a step away from gold was taken in the recent decision regarding central rates, when countries were permitted to communicate these rates to the Fund either in gold, SDRs, or another member's currency.

As long as gold and SDRs retain their fixed relationship, the expression of rates in SDRs is equivalent to their expression in gold. The expression of rates in current dollars, however, appears to be a more decisive step, lending substance to the belief that the world is now on the dollar standard. But this is an ambiguous term. The world is on the dollar standard in the sense that the dollar is not convertible into a final reserve asset, a situation that will continue for some time. But the world was at no time on the dollar standard in the sense that currencies (including the dollar) were not expressible in terms of a different numeraire. The Fund translates all rates, in whatever terms they are communicated, into gold and SDRs. Using market quotations of parities or central rates, the gold value of the dollar was at all times determinate; now Congress has approved the devaluation of the dollar (by 7.89 per cent), and the new gold value has been formally declared to the Fund.

What would be the effect of using the (current) dollar as numeraire? The United States would be unable to initiate a change in the exchange rate for the dollar by declaring a new par value (and would be unable to change the exchange rate by market intervention if the dollar remained the principal intervention currency). Any change in the par

value of the dollar would have to come about by unilateral actions of others (including decisions to let exchange rates float), or by multilateral negotiation. To be sure, a change in the exchange rate for the dollar did not actually come about without multilateral negotiation (and the mobilization of speculators) even when the current dollar was admittedly not the numeraire, before August 15, 1971. The reason was the overwhelming economic size of the United States. As long as this situation persists, any change in the value of the U.S. dollar in terms of other currencies could legitimately entitle many other countries to claim that they had thereby been placed in fundamental disequilibrium. Barring negotiation, they would be entitled to follow the United States to correct that disequilibrium. However, as the relative size of the U.S. economy continues to shrink, and as larger economic units emerge elsewhere in the world, this difference between the United States and other units will tend to disappear. Unless these large units allow their currencies to fluctuate vis-à-vis one another, big parity changes may have to be multilaterally negotiated, but, possibly, no small ones will have to be. And if it is not certain that a world of large economic blocs will be a world of floating rates, it makes sense to devise a system that gives each country the means to initiate a parity change. There is no reason to deprive the United States, even in principle, of the ability to take the initiative in changing its legal parity without the need for multilateral negotiation or the suspension of convertibility and threat of an international crisis.

A more difficult question concerns a possible break in the fixed relationship between SDRs and gold, which would make it meaningful to express parities in SDRs rather than in gold. If the SDR became the numeraire, countries could then change their parities without changing the gold price of their currencies—as long as no country maintained an official gold price. It has been suggested that this might make it easier for countries to change parities, since the same importance may not be attributed to the SDR value of a currency as to its gold value. This might no longer be the case, however, once the SDR became the numeraire of the system.

Breaking the fixed relationship between the value of SDRs and gold would imply the demonetization of gold, unless at least one country was willing to buy and sell its own currency for gold at a fixed price, and that currency was also acceptable to other countries as a reserve or intervention currency.

If SDRs became the numeraire for the system as a whole, it is still conceivable that a limited group of countries might continue to use gold for this same purpose and also as a means of settlement among them-

selves. They would then have to change the gold price whenever they changed the SDR price of their currencies.

The Role of the Fund

It has been suggested but not generally agreed that the role of the Fund should be strengthened. This means two things: (1) The Fund should continue to perform its present roles as a sort of credit cooperative, through drawings and repurchases, and as an international mint issuing SDRs, and, as administrator of a code of good behavior in international monetary affairs to be followed by individual members, its powers should be enhanced. (2) Decision making in respect of the major problems and crises of the international monetary system, including its reform, should take place substantively within the framework of the International Monetary Fund. An enhancement of its powers may be required to make some of the suggested reforms effective. As to decision making, the experience of recent years has shown that the Fund lacks an organ at the political level that can substantively decide major questions. By default, these questions have been taken outside the Fund to the ministers and governors of the Group of Ten, to the exclusion of the representatives of other members, the vast majority of which are LDCs. The full Board of Governors of the Fund, where members are represented by ministers and central-bank governors, is obviously too large for effective decision making.

As a solution to this problem, it has been suggested that a small committee of governors might be established which would be permanently on call to discuss issues that must be resolved at the political level. Such a committee would have no formal decision-making power, which would remain in the last analysis with the full Board of Governors, but a representative committee would have the moral authority to ensure that its recommendations were followed by the full Board of Governors.

Recent experience also suggests that it would be desirable to introduce somewhat greater flexibility into the Articles of Agreement. Care must be taken to avoid drawing the Articles so broadly that they become meaningless. But it should be possible to introduce into them somewhat greater scope for resolving certain substantive matters by the enactment of by-laws rather than amendments, so long as these by-laws can be changed only by very high majorities of the total voting power and by large numbers of members voting in their favor. In this way, the interests of the membership would be protected, but action could be taken quickly, without the lengthy ratification process in each country that is today necessary to change the Articles.

Further Outlook

The world may move gradually toward the system described in the preceding section. In several respects, that system would be more like the one originally envisaged at Bretton Woods than the one that has actually emerged over the last twenty-five years. The principle on which the system would function would still be the par-value system, although with new elements of flexibility. Parity changes would take place more promptly than they do now and would be smaller and more frequent. The world's owned reserves would be held not in national currencies but mainly, or at least increasingly, in SDRs—assets independent of the policies of national authorities; this would be closer to the Bretton Woods conception, with SDRs taking the place of gold. Intervention would still (most probably) take place in a few national currencies, so that working balances would almost certainly have to be held (and might even increase over time). In any case, convertibility, or—more precisely—regular conversion, would limit the issuers' ability to run deficits. Self-discipline would continue to be of prime importance, but the privileges of the reserve centers and others with privileged access to balance-of-payments finance would be reduced, and those countries would have to make a more timely contribution to the adjustment process. Even surplus countries might do so.

If the system developed in the long run toward using SDRs as an intervention currency, one would then have returned to arrangements resembling the classical gold-bullion standard, except that SDRs would take the place of gold, and parities would still be considered changeable in fundamental disequilibrium. Even the slight widening of margins would not be a radical departure from the gold-bullion standard, when some countries did play around with the gold points.

One could imagine an even more far-reaching development, with SDRs becoming a world currency—just as the dollar was (and may still be) on the way to becoming a world currency. In order to transform SDRs into an intervention currency, it would not be necessary to extend the range of permissible holders very widely—not widely enough to make SDRs a world currency. Nor should they become such a currency in the foreseeable future. The difficulties the European Economic Community faces in taking the first steps toward monetary unification—a more modest aim than instituting a single European currency—demonstrate the obstacles in the way of superseding national by world currencies. These difficulties, of course, reflect the fact that, as long as policy autonomy is not abandoned in other fields, it can hardly be abandoned in the monetary field. Even more to the point, countries do not want to abandon monetary autonomy.

What would be the effect on the international monetary system of a continuing trend toward the formation of larger regional economic units—a trend of which there are some signs today? Everything would depend on the considerations that gave rise to the formation of these units, and on their size and number. They would not need to be hostile blocs; they might emerge as natural developments, responsive to the advantages of economic or political integration. In units of this kind, monetary unification would be the *effect* of economic integration, rather than vice versa. They are likely to be units in which integration was brought about by a reduction in tariffs and other obstacles to trade within the unit, rather than by a joint defensive effort to raise barriers to economic intercourse against a hostile world.

In a world in which these friendly units were important, there might well be considerable room for changes in international monetary relations. But even a world with a few very large units could still wish to maintain stable rates. Under these conditions, the present international machinery could continue to function essentially as it does now. Exchange-rate changes, however, might have to be multilaterally negotiated, as was the recent realignment, rather than left to the individual decision of each unit, subject to surveillance of a general kind by the international financial community through the Fund.

Alternatively, if there were a few very large units, they could also decide to float against each other. The likelihood of genuinely free floats would be increased under these conditions, because the relative importance to each unit of relationships with other units would be smaller than it is for most individual countries today. This, in turn, might have repercussions on the international machinery for surveillance.

In the absence of a single currency inside each unit, the possibility of changes in the intra-unit rates would still be important. In consequence, there might be a need for surveillance over such rate changes and for institutions to supplement liquidity. It would seem natural that this task be taken over by regional institutions. But this would not necessarily be the case. Because each unit is likely to consist of one or a very few major countries, along with a large number of smaller ones, the latter might prefer that surveillance be exercised by an international rather than a regional institution, as a regional institution might well be too subservient to the major members inside the unit. Still, regional institutions would likely prevail.

On several occasions we have suggested that governments may falter on the path to an internationalist option. This is not the likeliest development. Even a collapse of the recent realignment need not bring it about, but such a collapse would be extremely dangerous. On the other hand, the

realignment may survive but be rendered less meaningful by the spread of controls. If the internationalist option were to be rejected, blocs would probably be formed. Since the motives leading to formation of the blocs would be defensive—especially in the absence of machinery for maintaining orderly exchange-rate (and trade) relations—these blocs would probably be formed by raising internal, rather than by reducing external, barriers. In such a world, exchange rates would in all likelihood continue to fluctuate, and it is unlikely that blocs and countries would submit to any effective international surveillance. As a result, the trend toward increasing integration of the world economy, which has served it so well in the postwar period, would be arrested if not reversed. The more rapidly progress is made on reform of the international monetary system, the less likely this development—delay could be extremely dangerous.

The failure of the internationalist option would be particularly dangerous for the less developed countries. They would be forced to unite with the defensive blocs formed by major countries. This, in itself, would tend to limit their access to markets, and their relative poverty would make such a development particularly hard to bear. Furthermore, the extent to which their voices would be heard inside each bloc, unprotected by surveillance on an international scale, would be less than at present. One could imagine the less developed countries inside each major bloc forming a defensive subregional bloc, but this would still be less than ideal in most cases.

The probable effects on the international monetary system of increasing integration of the European and Asian Communist areas into the international economy are too unpredictable at this moment to justify comment in this paper. As an oddity, it may be mentioned that the Articles of Agreement included a special clause to meet a desire of the Soviet delegation at Bretton Woods: Article IV, Section 6(e) exempts par-value changes from the requirement of Fund concurrence "if the change does not affect the international transactions of members of the Fund." It is difficult to imagine how, in the past or the present, there could be an economy so completely devoid of an effective price system that this clause would have practical application to it.

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