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United Nations Report on Measures for
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March 25, 1952

UNITED NATIONS REPORT ON MEASURES FOR INTERNATIONAL ECONOMIC STABILITY

Miroslav A. Kriz

Introduction

A new United Nations report on "Measures for International Economic Stability" 1/ formulates and analyzes "alternative practical ways" of maintaining a reasonable international balance--alternative to those put forward by an earlier United Nations report on "National and International Measures for Full Employment." 2/ The earlier report was debated at some length in the Economic and Social Council at its session in Geneva in July and August 1950, the United States delegation taking especially sharp exception to the report, 3/ and it was also discussed at length in academic journals. 4/ The new report will be debated in the Economic and Social Council in May. Pending this official debate, some comments are offered here in the belief that the new report explores more fully than has yet been done the "practical ways" that may reasonably be considered in dealing with the problems of international economic policy that are likely to arise if and when--perhaps in 1954--a military balance of power in the world is reestablished and the defense efforts of the United States and other nations can be relaxed.

The discarded formulae

To achieve international and external stability at full employment, the earlier United Nations report presented a comprehensive

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1/ "Measures for International Economic Stability", report by a group of experts appointed by the Secretary General (United Nations, New York, November 1951). The experts were: James W. Angell, Professor of Economics and Executive Officer of the Department of Economics, Columbia University; G. D. A. MacDougall, Fellow of Nuffield College and Reader in International Economics, Oxford University; Javier Marquez, Alternate Executive Director, International Monetary Fund, formerly Professor of Economics, National School of Economics, Mexico; Hla Myint, Lecturer in Colonial Economics, Oxford University, formerly Professor of Economics, Rangoon University; and Trevor W. Swan, Professor of Economics, Australian National University.

2/ "National and International Measures for Full Employment", report by a group of experts appointed by the Secretary General (United Nations, Lake Success, New York, December 1949).

3/ Cf. Economic and Social Council, Official Records, Eleventh Session, July 3-August 16, 1950.

4/ See C. P. Kindleberger, "International Disequilibrium," Canadian Journal of Economics and Political Science, November, 1950; W. W. Rostow, "The United Nations' Report on Full Employment," Economic Journal, June, 1950; Jacob Viner, "Full Employment at Whatever Cost," Quarterly Journal of Economics, August 1950; and H. C. Wallich, "United Nations Report on Full Employment," American Economic Review, December 1950, p. 876.

program for governments, acting both separately and through international institutions and conferences. There is no need to consider here the recommendations with respect to domestic measures for employment stabilization; it suffices to recall that these recommendations were centered upon the achievement and maintenance of adequate effective demand. Two main lines of approach were suggested--the first, by controlling investment through fiscal and monetary measures designed to stabilize private investment and through compensatory variation in public investment, and the second, by stimulating and stabilizing consumer demand, mainly through a variety of fiscal policy measures. For highly developed countries principal emphasis was put on the stimulating and stabilizing of consumer demand. Heavy reliance was placed upon fiscal policy, including measures to be brought automatically into operation by the fluctuations in an unemployment index.

The difficulty with these recommendations was that they were devised to deal with the problems of the great depression of the 'thirties rather than with those of the full employment of the 'fifties. (In fairness it must be noted that the report was prepared in mid-1949 when there were apprehensions lest the mild recession in the United States lead to a world slump.) They did not deal satisfactorily with the crucial problem of achieving a full-employment level of effective demand without precipitating inflation well before that level is reached and without impairing the economic efficiency of the country concerned. They treated the economic process as completely responsive to government regulation, and left aside the issues of political and economic freedom.

The recommendations with respect to international measures for the stabilization of employment were essentially three. The first was for an international conference to develop a joint program for "a new structural equilibrium in trading relationships." By exchanging and reconciling national foreign trade "targets", the participating countries were invited to "harmonize" their economic policies; and in order to implement these "targets", they were expected to adjust their production structures, import and export policies, etc. These recommendations therefore called for detailed foreign trade planning and specific economic direction; how these "targets" were to be implemented in free, or substantially free, economies was not, however, stated. Nor was it clear how foreign trade forecasts on a world-wide basis could be made more effectively than those by the Organization for European Economic Cooperation during the first year of its existence when "targets" were more often missed than hit (even allowing for a reasonable margin of error). Finally, even assuming that each country would be willing to disclose its real "targets", their international reconciliation would undoubtedly raise more delicate problems of international bargaining than any international conference has ever faced.

The second recommendation was a scheme for the stabilization of international trade. Under this scheme a country (in effect, principally the United States) that, as the result of a "general decline in effective demand," imported less than in an agreed "reference year" would be required to deposit with the International Monetary Fund an amount of its own currency equal to the fall in the value of its imports (less the fall, if any, in the value of its exports). Conversely, the countries experiencing a decline in their exports would receive from the Fund a special supplement of foreign exchange sufficient to make good the deficit on current account that would result from the continuation of the same volume of imports from a surplus country as in the "reference year". In effect, the surplus country would be required to replenish the foreign exchange reserves of the deficit countries by lending back to them any increase of its own gold and foreign exchange reserves resulting from a decline in its imports identified with a recession in its effective demand. This loan, or "deposit", would be repayable only if in a subsequent period its reserves were to diminish and those of the other countries were to increase.

The third recommendation was a scheme under which a country (i.e., the United States) undertaking long-term investment abroad would fix for five years in advance the annual total of its foreign lending on both public and private account and would make good through a separate account in the International Bank for Reconstruction and Development any deficiency in the actual flow of that long-term investment below the total fixed.

In suggesting these two schemes the report greatly underestimated the technical and operational difficulties involved, as well as the political difficulty that the government of a surplus country like the United States would face in making a large and indefinite commitment for foreign aid. Furthermore, the possibility that a country might step up its imports by simply tolerating domestic inflation was entirely discarded; nor was there any consideration given to the question of whether automatic trade-deficit financing would not interfere with the export incentives of the deficit countries. Briefly, "the formula whereby the report would make countries suffering from a decline in effective demand responsible for the deficits to be produced in other countries" appeared "an arithmetic rather than an economic solution of the problem. Surely responsible policy makers would not be content with such a generalized, mechanical formula without examining the circumstances of the particular case." 1/

As already noted, the report was discussed in the Economic and Social Council at its eleventh session in Geneva in July and August 1950. It met with substantial criticism; 2/ more particularly, the United States

1/ John H. Williams, "International Trade Theory and Policy--Some Current Issues", Papers and Proceedings--American Economic Review, Volume XLI, No. 2, May 1951, page 429.

2/ Official Records, Eleventh Session, July 3-August 16, 1950.

representative stated that the United States Government "was not prepared" to enter into any commitment "automatically to provide indefinite amounts of public funds over long periods"; and "was unable to accept the experts' proposal that countries suffering from depression should be obliged automatically to deposit their currency with the Fund, and that other countries should have automatic drawing rights on such countries in accordance with a predetermined formula". 1/

As a result of this debate, the Council adopted a resolution on full employment which, with an accompanying set of recommendations, requested the Secretary General to appoint a further group of experts "to prepare a report ... formulating and analyzing alternative practical ways of dealing with the problem of reducing the international impact of recessions that may arise." This group met under the chairmanship of Professor Angell, with Mr. G. D. A. MacDougall as British representative; its report issued on its own responsibility (hereinafter called the Angell report) is the subject of the rest of this paper.

The "Alternative Practical Ways"

The Angell report is not concerned directly with the maintenance of full employment and the establishment of a new equilibrium in world trade and payments. It assumes as a working hypothesis that the major countries have "both the will and the means to avoid deep and prolonged depressions" (Para. 1). However, in the existing precarious state of world economic balance, even minor disturbances in some countries (the United States is clearly intended here)--"disturbances which may often be inseparable from the economic progress itself" (Para. 2)--may give rise to major repercussions elsewhere. Although today's problems are not those of a recession, disturbances in international payments consequent upon a sudden cutback in government expenditures two or three years hence are a distinct possibility, as already noted; and for this reason the Angell group's working hypothesis is a plausible one. Nevertheless, as I shall point out in the final section of this paper, the problem of international economic balance is by no means solely one of the impact of a deflation or recession in the United States on the outer world.

Yet, this is exactly the Angell report's starting point, while its fundamental postulate is that a workable international economic system can be established provided there is no decline in effective demand in the United States; if effective demand is maintained, independent fluctuations elsewhere can be coped with more effectively. This postulate is, however, acceptable within definite limits only, as care must be taken not to exaggerate the size of the United States economy or its impact on world economic conditions. With these qualifications and reservations, this postulate appears therefore realistic. The report expresses it in numerical terms by noting that if a new recession had the same proportionate effect on the United States' foreign payments as in 1937-1938, 2/

1/ *Official Records*, Eleventh Session, July 3-August 16, 1950, pages 125 and 126.

2/ In the recession of 1937-38, employment in the United States fell by 4 per cent, but the annual value of United States merchandise imports dropped by 36 per cent.

the dollar income of the outside world would be reduced by as much as 10 billion dollars. In fact, as happened in 1949 and 1951, the movement of inventories, along with the tendency for the actual consumption of some imports to vary more than proportionally with employment, and the associated price changes, may considerably affect the value of United States imports even if the level of employment remains generally steady.

If only relatively minor setbacks to employment and output in large parts of the world can be reasonably expected, as under the Angell report's working hypothesis, the problem of international economic instability becomes a "manageable" one. Acute problems can, of course, emerge from crop fluctuations and other irregular movements in the supply of, or the demand for, particular commodities and from the associated price changes. Nevertheless, with a reasonably high and steady level of employment in major countries, some of the intractable problems of international economic instability can be dealt with in a practical way.

The measures that can be reasonably devised and effectively implemented under constantly changing conditions are not "of a kind which can be expressed in any definite formula" (Para. 50). For this reason the recommendations of the earlier report regarding the availability of a steady flow of foreign exchange on current account and on long-term capital account are referred to only very briefly in the Angell report; and it is noted that they "did not commend themselves to governments as acceptable or practical" (Para. 26). As the Angell report succinctly puts it:

> We have been concerned to suggest policies which would help to improve international economic stability, and to discuss the conditions under which such policies might be made practicable and effective, rather than to draw up blueprints for rigid and automatic stabiliziation devices. The simplicity of such devices is often more apparent than real; and no set of fixed rules can successfully replace the exercise of responsibility and discretion by the appropriate national and international institutions. [Para. 27]

Not only does the Angell report discard rigid and automatic stabilization devices, but it also refrains from stating, or even implying, the views fashionable in certain quarters to the effect that "many of the world's troubles would be eased if one country would assume unilaterally the burden of international stabilization and meet the costs as they arise" (Para. 51). On the contrary, the instabilities of international relationships can be kept within manageable limits only if most countries are prepared to play their "several parts". These general considerations are not further elaborated; nevertheless, they are an essential qualification to the report's working hypothesis that the main problem to be faced is a decline in effective demand in the United States.

Finally, the Angell report does not put forward categoric recommendations. Since fresh judgments of facts and policy alternatives are required at every turn, the report merely formulates basic considerations that should guide policy decisions by governments and international institutions. These considerations, which now will be discussed, concern: (1) the formulation and operation of international commodity arrangements; (2) the countercyclical flow of international capital; and (3) the strengthening of international monetary reserves.

International commodity arrangements

The first group of considerations concerns the international impact of short-term fluctuations in the prices and terms of trade of primary products. This facet of international economic instability was not examined in the earlier report, which as already noted was concerned primarily with the maintenance of employment and incomes in the major industrial countries, especially the United States. This onesidedness was much criticized at the Eleventh Session of the Economic and Social Council, more particularly by Brazil and India; and it was as a result of this criticism that the Council's resolution called expressly for "alternative practical ways" to deal with the problem of reducing the vulnerability of underdeveloped economies to fluctuations in international markets. In addition, another group of experts was appointed to report on the measures for the economic development of underdeveloped countries. 1/

The broad terms of reference assigned by the Economic and Social Council to the Angell group could be interpreted in either of two ways. A somewhat literal but far-reaching interpretation could have led toward the proposing of an international "parity price" scheme for raw materials and other primary products. This would have involved the permanent operation of international controls over the production of primary commodities (including such measures as acreage allotments) and the allocation of the commodities--indeed, a controlled world economy for primary products. The Angell group discarded, however, such a scheme as neither practicable nor desirable; and adopted instead an approach aiming essentially at nothing more than the smoothing out of the sharp short-run fluctuations. In order to balance supply with demand by encouraging or discouraging consumption or production, price changes need not be nearly so great as they in fact are, according to the Angell report; indeed, much smaller changes would obviate unnecessary and wasteful fluctuations in new investment in primary production and in the output of primary products. However, the suggestions put forward in the report:

1/ Cf. "Measures for the Economic Development of Underdeveloped Countries", report by a group of experts appointed by the Secretary General (United Nations, New York, May 1951).

do not attempt to make the average price over a period of years higher or lower than it would otherwise have been. Their objective should be merely to reduce fluctuations around the long-term trend. /Para. 70/

The only "practicable method" of reducing the international impact of short-run fluctuations in the primary-commodity prices and terms of trade is "a direct and detailed attack on the problem through the negotiation of international commodity agreements" (Para. 29). This idea was much discussed in the 'thirties and again during the postwar years; but the record of achievement has been small. Nevertheless, for two reasons a new attempt should now be made, according to the report. First, the long-term trend of commodity prices is more likely to be upward than downward; and burdensome commodity surpluses such as those of the 'thirties are now unlikely because of the faster rate of expansion in world industrial production than in the output of primary products. An expanding world economy thus seems to have removed one fundamental obstacle to commodity agreements; the Havana Charter of 1948, which considered such agreements almost wholly in terms of burdensome surpluses, has been by-passed by the course of events, according to the report. This, I believe, is very much to the point. The growth of demand for industrial raw materials and for basic foodstuffs appears as a direct outcome of the full-employment policies pursued by the industrial countries of Western Europe and the United States as well as of the political awakening of the primary-producing countries.

A second reason put forward in the report for reconsidering commodity arrangements is the practical experience gathered from the operation of the International Wheat Agreement and from the United Kingdom's long-term contracts; despite their complexity and notwithstanding the difficulty of reaching agreements regarding prices and quantities and their fluctuations in the future, these programs have been put in operation and have not broken down.

A wide variety of arrangements is regarded as suitable for the different types of commodities, including long-term agreements on quantity and price, either bilateral or multilateral (like the International Wheat Agreement), long-term contracts, and buffer stocks, either alone or in combination. The report warns, however, against the allocation of maximum production quotas (on the ground that these tend to freeze the geographical pattern of production) and against the allocation of import quotas (since restriction of consumption should be avoided except in cases of international emergency).

The report revives a suggestion to which the League of Nations' Delegation on Economic Depressions attached considerable weight, namely internationally-financed buffer stocks. 1/ Capital finance for buffer

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1/ Cf. "Economic Stability in the Post-War World", report of the Delegation on Economic Depressions (League of Nations, 1945, pages 265 and 313).

stocks should be provided largely from the countries chiefly concerned (a difficult proposition under conditions of inconvertible currencies, arbitrary exchange rates, and artificial prices), but it would be useful to have a supplementary international source of finance. The report suggests that the International Bank for Reconstruction and Development might be willing in principle to consider assisting in the financing of buffer stocks, as a means of promoting satisfactory conditions for economic development. It might be possible for the Bank (or some other international authority) to provide funds for the various buffer stocks on, say, a 50-50 basis; and in raising any necessary loans itself, to pledge as collateral the total stocks of goods held.

This approach appears, on the whole, a realistic one, all the more so because its limitations are clearly set forth. International commodity arrangements are notoriously difficult to organize and to operate. Furthermore, they would not, of themselves, stabilize either producers' income or exporting countries' foreign exchange receipts against fluctuations in the supply of the commodities concerned. Finally, even if it were possible to make arrangements for the twenty-five primary commodities most important in value in world trade, only one third of the total would thus be covered. Commodity arrangements might therefore merely reduce the world trade instability. Nevertheless, by concentrating on a small number of important commodities subject to the most violent fluctuations, it should be possible to make a substantial contribution to stability.

The international flow of capital

The second group of considerations put forward in the Angell report concerns the international flow of capital. "Rigid stabilization of the total flow of long-term capital from each country does not seem practicable or even necessarily desirable" (Para. 31). It is important, however, that countries in the process of economic development should be able to maintain a steady level of development even in the face of an incipient economic recession in major industrial countries. This can be achieved only if a fall in primary commodity exports, and therefore in foreign exchange earnings, can be prevented from reducing the developing countries' imports; and this in turn can be achieved only if the inflow of foreign capital not only does not dry up, but actually is increased despite the adverse circumstances. On the other hand, for the lending (capital-exporting) countries, the maintenance of a steady volume of exports for economic development helps to support domestic employment and thus combat the recession, according to the report; however, since private capital is likely to be reluctant to flow abroad under conditions of depression, it is desirable for the industrial countries that countercyclical lending be undertaken by the governments themselves either directly or through international institutions.

The idea of countercyclical foreign investment, like that of buffer stocks, was originally put forward by the League of Nations' Delegation on Economic Depressions; but although it was strongly supported by

Professor Viner and others, it apparently did not appeal particularly to the international planners during the postwar years. The charter of the International Bank for Reconstruction and Development requires it to lend when suitable borrowers appeal for its aid, but there is nothing in it that indicates that the Bank could properly make timing with respect to the business cycle an important consideration in granting or withholding loans.

It is presumably to correct this state of affairs that the Angell group suggests that:

> all governmental or intergovernmental agencies which supply capital funds for foreign economic development should be prepared to vary the rate at which they provide these funds, in the light of fluctuations in the foreign exchange receipts of the borrowing countries on current account and on other capital account and within a total burden of external debt which the borrowing country can reasonably assume. [Para. 95]

In the event of a recession, the International Bank for Reconstruction and Development ought therefore to stand ready to expand greatly the rate of its disbursements on outstanding loan commitments and to make additional loans without undue delay to member countries for development purposes. Furthermore, in cases where there may be an agreed development program in which the Bank as well as private foreign capital is participating, the Bank should give consideration to increasing its own participation, whenever there is a decline in the volume of private foreign investment, through loans to government or semi-government institutions (the Bank obviously could not take over the providing of capital previously supplied by foreign equity investment).

For such countercyclical foreign investment to be possible, several conditions must be fulfilled. First, if the rate of the Bank's lending is to be expanded at a relatively short notice, a general development program must be prepared well in advance--a difficult prerequisite, as experience in many underdeveloped countries shows, but an essential one if funds are to be spent intelligently and effectively. Secondly, the total debt burden assumed by a country should not exceed some reasonable limit; how to determine this limit, the report refrains from stating, except that the stage of development reached by the country concerned and its general prospects appear as essential criteria. Thirdly, if the International Bank is to be ready to expand its lending in the event of a recession, for the purpose both of long-term investment and of the financing of buffer stocks, it may need larger and more flexible resources than it has today.

Under its articles of agreement, the International Bank can use only 20 per cent of its subscribed capital for making loans, any additional lending having to be financed through the sale of securities. Unless it conserves a substantial amount of liquid funds borrowed during good times, the Bank would therefore have to increase its security sales during recessions when private investors may not be particularly anxious to buy securities related to foreign undertakings. "It is hence clearly undesirable that the Bank should continue to be so heavily dependent on so inelastic a source" (Para. 105).

Four possible lines of solution are suggested: The first is to increase the proportion of the Bank's capital that is actually available for making loans. Under the existing statute, 20 per cent of the subscribed capital is paid in; 18 per cent of this is payable in the member's own currency but is available for loans only with the approval of the member in each case. Members might therefore approve releases of larger amounts than in the past, but such a step would not yield considerable funds. The second possibility is to increase the proportion of the paid-in capital, i.e., the 20 per cent referred to above; and to the extent that the members approve the lending of their currencies, the Bank's available resources would be increased. Thirdly, "in the event that the Bank encounters difficulties in placing its securities with private investors, it might borrow from the governments or central banks of the lending countries, under conditions safeguarding the interests of private holders of Bank securities" (Para. 106). Unlike the two previous possibilities, the third would not require an amendment of the articles of agreement; but it would require national legislation in some cases to enable the central banks to hold the International Bank's bonds. Whether such a recourse to central bank financing would be wholly desirable is of course another matter. The fourth possibility is to increase the Bank's total subscribed capital. This step will in any event be necessary when the Bank approaches the limits of its power, now fixed by its articles of agreement, to borrow and to guarantee.

These policy alternatives appear reasonable on the whole. There is nothing in the Angell report that would suggest that the International Bank should in any way relax the standards of its lending; and the limitations and the difficulties of countercyclical lending are set forth openly and frankly. Clearly, the International Bank could not have refrained during recent years from financing acceptable projects merely because of the prevalence of a high level of employment in the United States and Western Europe; nor can it regard the possible countercyclical effects of its lending upon the industrial countries as the only element in its policy decisions. "How far the International Bank for Reconstruction and Development may be able to expand its lending in the event of a recession depends entirely on its success in finding credit-worthy borrowers and on the practicability of its gaining access to a more flexible source of funds" (Para. 36).

<u>International monetary reserves</u>

The third group of considerations concerns ways of increasing international monetary reserves. According to the report, the total reserves of countries other than the United States are inadequate because they are now "much smaller" in relation to trade than before the war. The International Monetary Fund provides only "a comparatively trivial" supplement to international reserves (Para. 119), assuming no waiver of the rule limiting members' annual purchases of foreign currencies to 25 per cent of their quotas. Moreover, the Fund's holdings of gold and dollars (2.8 billion dollars):

> might suffice to offset fluctuations in United States imports as great as those in 1949, but a twelve-month reduction in dollar supply of the same relative severity as that in 1937 and 1938, even if followed by a quick and full recovery in the following twelve months, might well mean a reduction of as much as $10,000 million in the supply of dollars over the whole period of two years. Even assuming that countries had previously been running a surplus in their balance of payments with the United States (as many had for a short time before mid-1951), that they could use a part of their own reserves, and that United States export prices might fall to some extent, the remaining reduction in their dollar purchasing power would be far larger than could be met by the Fund's present resources. [Para. 115]

As remedies for the inadequacy of international reserves, even as supplemented by recourse to the Fund, the Angell report examines three possible methods. First, the price of gold might be raised uniformly in terms of all currencies, as provided for in the Fund's articles of agreement. The report discards this method on the grounds that "a change in the price of gold raises many political problems" (Para. 121), but the balance of its economic argument for and against a world gold price rise is not as clear-cut as I would wish. For instance, it is asserted that, measured in dollars, the official gold price is no higher than before the war, while prices in international trade have doubled; the monetary reserves therefore can serve as a buffer only against trade fluctuations that are much smaller than formerly. However, this contention is statistically correct only if a post-1934 year is selected as the base; if a year prior to the 1934 dollar devaluation is taken as the base, the result obtained is different: compared with 1926 levels, wholesale prices in the United States in December 1951 were 77 per cent higher and the gold price 69 per cent higher. Furthermore, the implication that the increase in the prices of internationally traded commodities should be offset by a gold price rise rests on the assumption that gold itself is a commodity and not a monetary metal--an assumption that has often and convincingly been challenged. It is also asserted that a higher gold price, by stimulating gold production, would not be wasteful since only a small fraction of world's resources would be involved. What matters, however, is not the proportion for the world as a whole, but that for the various gold-producing countries. The Angell report likewise seems to underestimate the complications that a gold price rise, with its real and psychological inflationary consequences, would add to the task of monetary management in many countries. I have recently dealt elsewhere in some detail with the so-called world gold price problem; 1/ and the remarks made here are therefore intended to register the particular criticisms without discussing them in any length. I wholeheartedly agree with the very pertinent argument that:

> The benefits of a higher gold price would be uneven. Countries with low gold reserves would gain little; those with high reserves, or with a substantial gold-mining industry, would gain disproportionately. There is also a danger that some countries would soon spend the increase in the value of their reserves, rather than keep it as a buffer against trade fluctuations. /Para. 120/

The second possible method of increasing reserves consists of bilateral arrangements, such as stabilization credits from one country to another, and the mutual granting of lines of credit to cover swings in the trade balances between two countries. The report does not discuss these, on the ground that an international report should be confined to multilateral arrangements. This is an omission that must be regretted since it would have been of some interest to have the Angell group's views as to the economic policies that would be essential as prerequisites for intercentral-bank or intergovernment stabilization credits.

The third possible method of increasing reserves consists of multilateral international arrangements of various types. Funds could be made more or less unconditionally available to meet deficits, within specified limits, as in the European Payments Union. Funds could conceivably be made available, in amounts determined by more or less precise rules, agreed upon in advance, under which, in accordance with the earlier United Nations report's proposals, countries suffering from a fall in their own effective demand would make their currency available to the rest of the world. Finally, funds could be made available by an international authority at its discretion, limited only by agreed general principles and by its total resources, as in the case of the International Monetary Fund.

In weighing these three alternatives, the Angell report formulates three criteria that should guide the policy decisions regarding any addition to international monetary reserves:

> We have been influenced, first, by the difficulty of formulating precise rules in advance. However carefully these may be devised, they will often be inapplicable to future situations. /Para. 123/

1/ Cf. "Is There a World Gold Price Problem Today?", Paper Prepared by M. A. Kriz at Federal Reserve Bank of New York for Presentation at Third Meeting of Experts of the Central Banks of the American Continent, Havana, Cuba, February 25, - March 7, 1952.

> Second, we are impressed by the need to make finance available as quickly, as cheaply and as freely as possible at the onset of a recession, to prevent an unnecessary contraction of trade. /Para. 124/
>
> Third, we recognize that the provision of the necessary additional international reserves must include the extension of credit through international institutions by those countries whose currencies are chiefly needed and acceptable. At the present time, the need is primarily for United States dollars. Additional dollar resources are, however, unlikely to be provided, at least to meet what are regarded as normal fluctuations, unless there are firm assurances that the resulting contribution to international reserves will not be dissipated but will constitute a truly revolving fund. One way of ensuring this would be to exercise a strict control of the use of the resources, but this would run counter to the second principle mentioned above. A better way, we believe, would be the enforcement of more definite provisions for repayment of any funds drawn. /Para. 125/

To increase the international monetary reserves, the International Monetary Fund, "a workable instrument", should be used, according to the report. Certain changes in its structure and policies will be required, but:

> This does not necessarily imply that policies hitherto adopted /by the Fund/ have been mistaken, but rather that they may have to be different in the situation we are considering--a recession in one or more major countries that sharply, though only temporarily, reduces the demand for exports from most of the world. Some of the changes we suggest may, however, be useful even should this situation not arise. /Para. 126/

Some changes in the Fund's structure and policies can be made without requiring additional finance, the provision of which "raises special political difficulties". In the event of a recession, the Fund should be prepared to waive freely the rule that limits annual drawings to 25 per cent of a member's quota. At the same time, firm (contractural) repurchase provisions should be agreed upon in order to diminish the danger that currencies in greatest demand (actually, the United States dollar) would be either irrevocably lost or unequally distributed. 1/ In order

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1/ The present arrangements should be retained under which a country that has sold its currency to the Fund (that is, has borrowed) is to repurchase it (that is, repay it) when, among other conditions, its reserves increase, but the Fund "in appropriate circumstances" should also agree with members on fixed dates for contractual repurchase. The present repurchase obligation is indefinite in the sense that a member has a specific obligation to repay only in consequence of possible future increases in reserves. On the other hand, the procedure referred to above would permit the establishment of a firm commitment to repay at a specified date or dates.

to increase the willingness of the prospective borrowers to have recourse to the Fund, the latter might be given the authority to postpone repurchase obligations if, in its opinion, a "normal" situation had not yet been restored after "a substantial fall in the international disbursements of an important country or countries below what was regarded as a normal long-term level" (Para. 130). Furthermore, it might be possible for the Fund, in case of sharp short-term fluctuations in international trade, to spread the compulsory repurchase over a period of time. The Fund might also defer enforcement of the present rule obliging members, at the end of the financial year in which they have borrowed, to repay one half of the amount borrowed even if their reserves have remained constant during the year. Finally, the Fund might allow repayment in the currency borrowed, instead of the present obligation to repay in gold or convertible currency even currencies other than dollars.

It will be interesting to observe the Fund's response to these suggestions. Some of them raise legal and operational questions, others are on the borderline of policy; but the difficulties, although real, are not insoluble. However, other views put forward in the Angell report raise more fundamental issues. The Fund should give "the benefit of the doubt" to a member requesting assistance in case uncertainty exists as to the member's ability to repay. "If the Fund finds it hard to make such an estimate, it should in general accept the judgment of the member, provided the latter makes a definite repurchase commitment" (Para. 134).

In making any estimate of the future average exchange receipts of a member, the Fund, according to the report, should discard the possibility that a recession in a major country may develop into serious depression. Nor should the Fund, at the onset of a recession, attempt to conserve its resources for use in a possible major depression. "There would be no purpose in withholding resources when they are needed in order to use them when it is too late" (Para. 135).

On the other hand, the report maintains that the Fund should not refuse assistance to a member suffering from a temporary fall in exports to a major country, merely on the grounds that no serious unemployment has developed there and that a reduction in output, prices, or inventories represents a healthy readjustment. Clearly, this is a generalization of the situation that prevailed in the United States in mid-1949 when inventory changes were accompanied by a decline in imports and prices.

The Fund, it is held, should not refuse assistance to members that are pursuing restrictive or other policies that might be regarded "as not in keeping with the Fund's long-run objectives" in cases where refusal of aid would force the member to adopt even tighter import restrictions or suffer unemployment and so defeat the Fund's purposes. "Assistance should be forthcoming to a member, whatever restrictions it is imposing, provided these are not intensified" (Para. 137).

While these general policies could be carried out with the Fund's existing resources, these policies are not regarded as adequate to cope with recessions approaching the severity of the United States recession in 1937 and 1938. For this reason, there is a case for increasing the Fund's resources. This could be done through an increase in members' subscriptions, although it would not be necessary to increase all quotas in the same proportion. If an increase in subscriptions proved impracticable, reliance would have to be placed on the borrowing powers of the Fund. The United States, if it were to increase its subscription to the Fund or lend to it in the event of a major recession, might prevent unemployment in its export industries, reduce the need for other countries to take new discriminatory measures against its exports, and give effect to the spirit of its international full-employment commitments (Para. 34).

The views briefly sketched here call for a thorough discussion, but one that is outside the scope of this paper. The crux of the problem is how to give to Fund members the benefit of the doubt and how to provide assistance on the mere condition that existing trade and exchange restrictions be not intensified, and at the same time ensure that the ultimate goals of convertibility and multilateralism will be promoted. Regardless of this problem, however, the Angell report's advocacy of an increase in the Fund's resources while its discretionary powers are safeguarded deserves thorough consideration, the more so because it appears reasonable and practical.

A preliminary appraisal

In discussing primary-commodity arrangements, the countercyclical flow of international capital, and possible ways of adding to international monetary reserves, I have already commented on various specific issues raised in the Angell report. What remains is a preliminary appraisal of the report as a whole.

As discussed in an earlier section of this paper, whether the "alternative practical ways" are really practical, I have noted that the Angell report is almost exclusively concerned with no particular aspect of international economic fluctuations, namely the external impact of a decline in effective demand in the United States. This, of course, is an important factor in changes in the national incomes, the balances of payments and in monetary reserves, but it is by no means the only factor determining the international gold and dollar flow. The Angell report points this out in general terms, as noted earlier but not specifically. First of all, there are only very few countries whose exports to the United States provide the main support of economic activity; in most countries, total national income is less variable than the income derived from the direct trade with the United States. Furthermore, erratic capital movements, crop fluctuations, and changes in the terms of trade between primary-producing countries and the industrial countries give rise to international fluctuations that are entirely independent of the level of effective demand in the United States and which cannot be countered by increasing the latter. Finally, it is not only by the mechanistic channel of a falling-off in United States imports that the fluctuations in the United States economy are transmitted to the outer world. They are transmitted much more quickly, and in the initial stages more effectively, by their effects on business sentiment. True enough, in a world with inconvertible currencies and "controlled" capital movements (even if these actually are controlled only very imperfectly) there is no single business cycle for the whole world trading area. Nevertheless, it is a matter of common observation that business fluctuations and expectations in the United States even now have great influence on business expectations in large parts of the world.

In all fairness it must be stated that the destabilizing influence of the United States is not overstressed in the Angell report, as was clearly the case in the earlier report. 1/ There is, of course, no question but that the cyclical variation in the value of United States imports (and, to a distinctly lesser extent, in their volume as well), together with the building up of inventories during one phase of the cycle and their reduction during the other, exerts powerful effects on the outer world, especially on the primary-producing countries. Nor is it possible to deny the special responsibilities of the United States for the maintenance of reasonable international economic balance. Nevertheless, the influence that the United States exerts on the outer world is to a considerable extent attributable to the mere fact that a large portion of United States imports consists of raw materials that have a high cyclical amplitude of variation in price and that the fluctuations in demand for a particular import commodity can vary more than proportionally with employment. This high amplitude depends, of course, on the well-known fact that inventory fluctuations and the demand for particular import commodities are far more pronounced than fluctuations in economic activity in general. This, therefore, is not a special characteristic of the United States economy, but is true generally of industrial countries with large imports.

Altogether apart from the cyclical fluctuations in inventories, imports, and industrial production, the American economy exerts an influence on the outer world because of its greater flexibility and efficiency--and shall I say also its vitality. For there is little doubt that some of the dollar problems of the world are attributable to the high productivity of the American economy and the speed with which it exploits technical innovations, as will be pointed out later. The Angell report refers, it is true, to "disturbances that may often be inseparable from the economic progress itself" (Para. 1), but it neither expands this consideration nor draws any conclusion from it.

1/ Such exaggeration is made, for instance, when the size of the United States economy is measured by its share in world <u>industrial</u> production, rather than in <u>total</u> production, or by its share in world <u>exports</u> rather than in world <u>imports</u>.

While almost exclusive emphasis is placed in the Angell report on deflationary influences that the United States may exert on the outer world, almost nothing is said of the obverse case of the inflationary influences that may prevail in foreign countries and lead to an increase in their demand for imports from the United States. Indeed, the only mention of the problem of inflation and internal economic balance generally is that "nothing in the approach we have suggested will relieve any country of the responsibility of limiting its demands for consumption and investment to the total of the resources available to it, if it is to avoid inflationary pressure" (Para. 37). The consequences of a lack of internal balance for external equilibrium are not explored. Yet, as experience shows, a deterioration in a country's balance of payments may be due not only to deflationary influences from abroad, but also to inflationary influences at home. The Angell report thus displays a lack of balance in its conception of the problem of international economic balance and in its formulation of policy considerations.

That international payments of a country can be unbalanced because its currency is weak is a matter of common observation. Conversely, if and when domestic inflation is overcome, the effect on the balance of payments position may be striking. The postwar currency experience of Western Europe offers several examples of balance of payment crisis amidst domestic inflation, followed by a recovery in the international position accompanying the reestablishment of a reasonable monetary stability at home. The critical phase of the balance of payment difficulties of Western European countries came in most cases at a time, as in 1949 and 1951, when inflationary pressures in the United States had somewhat subsided but were continuing elsewhere; however, in the individual countries the balance of payment difficulties came to a head at different times that depended on the severity of inflation and on the speed and resoluteness with which countermeasures were taken. As a rule, these countries were in deficit in their international payments not only with the United States but also with every other major area of the world. Despite the postwar monetary experience, however, no consideration is given in the Angell report to the impact on international payments of the existence of a slower rate of inflation in the United States than elsewhere, or of the subsidence of inflation in the United States while inflationary pressures continue elsewhere. Yet, it is this slower rate of inflation or this subsidence, rather than deflation, in the United States that seems to have exerted adverse effects on the balances of payments and gold and dollar reserves of foreign countries in 1949 and 1951.

The Angell report also attaches considerable importance to the "indirect effects of fluctuations in effective demand in a major industrial country" (i.e., the United States) on the rise in primary commodity prices and hence on the terms of trade of the "other" industrial countries (i.e., industrial Western Europe). It rightly points out that "neither of these indirect effects can be overcome by the mere assurance that a country in which a recession originates will maintain its flow of foreign exchange to the rest of the world..." (Para. 25); it does not, however, note that increases in wages and other costs were as a rule a more powerful inflationary force in Western European countries than increased import costs; and that although the terms of trade appeared to have worsened by practically the same extent in France, Germany, Switzerland, and the United Kingdom, and to a somewhat smaller extent in the Netherlands, some of these countries lost gold and dollar reserves while others gained; in the latter countries the deterioration in the terms of trade was offset by heavier exports.

Another aspect of the Angell report that I would wish to qualify is its exclusive emphasis on international liquidity. The report is essentially a short-run program of action; but it seems to present that action as conducive, by itself, to lasting international balance. There is no warning that the international payment difficulties also reflect deep-seated economic maladjustments; and that a realistic step-by-step approach to better international balance requires not only additions to international liquidity but also structural readjustments in the productive capacity within countries and in the patterns of trade among countries. I am fully aware that the problem of establishing conditions conducive to higher economic productivity and efficiency was outside the terms of reference of the Angell group; what I miss in its report is any indication that the policy considerations put forward concern merely one aspect of the problem the world is facing.

To sum up: notwithstanding the Angell report, the problem of international economic stability is only partly the maintenance of adequate effective demand in the United States; it is also one, in the short run, of the monetary stability and, in the long run, of the economic productivity, of the outer world. The international payment difficulties, far from arising solely from the cyclical swings in United States economy, are also the result of the relatively larger real resources and higher productivity of the United States than of the rest of the world, and partly also of the smaller degree of inflation in the United States than in most other countries. The insistent demand for improvement in living standards, the pressure of economic development, and the requirements of defense are likely in other countries to exert inflationary pressures that will very probably be much greater in terms of their resources and productivity than comparable pressures in the United States. For these fundamental reasons, while the "alternative practical ways" of the Angell report represent a marked advance in realistic approach to intelligent and effective international economic policy--the hard core of the problem of reconciling international economic balance with internal economic balance under a steady and high level of employment in individual countries as a whole remains. Nevertheless, the Angell report is, within its terms of reference, an eminently reasonable step forward in attempting to deal with the particular problem of reducing the international impact of recessions that may arise in the next few years.