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The inability of the Bretton Woods monetary system and the British Search for a new international economic framework in the 1950's

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Summary

How is the reality of the Bretton Woods system and "embedded liberalism" ideology immediately after the Second World War II? What is the meaning of European integration in relation to the international economic regime? To approach these questions, this paper, taking the two UK proposals of floating rate and sterling convertibility – "Operation Robot" and "Collective Approach" – , argues, because of the ineffectiveness of both Keynesian policy and the IMF, in the 1950's, some of the UK policy-makers try to apply more market-oriented policy to resolve balance of payments crisis, but rejected by those who thought market solution expose the welfare state in danger. This paper also analyses reaction from the continental Europeans. Although they too recognized the limit of the IMF, and Marjolin was even looking for new Atlantic framework, their idea was not corresponded to the "Collective Approach". What they want was the convertibility through existing EPU framework, which is more reliable and effective than the IMF.

Introduction

0.1 "Embedded liberalism" in the Bretton Woods system[2]

Global financial crisis revealed vulnerability of the international monetary system basing on dollar and floating rate. On the other hand, European monetary cooperation which was actually developed from the 1970's basing on fixed exchange rate system as a defence from dollar based international system are also facing its limit. Rather than taking place dollar as a core currency, euro itself is facing the critical phase. In the discussion on Euro, much attention was paid to the problem of huge budget deficit and public debt to save the Euro, calling for balanced budget even though it means adoption of deflationary policies. On the other hand, proposal of strengthening of EU power to national budget policy too was a product of unanimity. This controversy on external

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1 I am very grateful to Professor Eiji Ogawa, Professor Sahoko Kaji, Mr. Hideki Hayashi, Professor Yuichi Kanai, Professor Naoki Fukuzawa, Professor Ken Fujita for their comments, criticism and advises, though all the errors remain the responsibility of the author.

2 There is controversy over the application of the expression "Bretton Woods system" to international monetary system in the post-war era. However, in this paper, I will not investigate in this argument further, and employ expression "Bretton Woods system" referring to the post-war international monetary order in which the IMF was assumed to play a crucial role. As to the argument over the expression of "Bretton Woods system", see Hiroshi, Makino, *Nichi-Bei Tsuuka Gaiko no Hikaku Bunseki: Nixon shock kara Sumisonian Goui made* (Comparison of monetary diplomacy in Japan and the United States: from Nixon shock to the Smithsonian Agreement), Ochanomizu shobo, 1999, pp.44-49.

monetary goal and national policy autonomy remains of the argument on the construction of post-war international economic framework. In the period, the central problem was how to establish an international framework in which both external liberalisation and domestic policy goals could be achieved without contradiction, though the weigh was more on the protection of national policy autonomy tempering the monetary stability. Thus, looking back on the Bretton Woods era might have some insight to the current issue on Euro, though not directly give any answers.

Mundell-Felming Trilemma pointed out three policy goals which could not be sustained at the same time: fixed rate of exchange, free movement of capital, and monetary policy autonomy[3]. All these three could not be achieved at the same time – any one of them must be sacrificed to achieve the remaining two. The classic gold standard of 19th century was stable, for each country was cooperative to maintain fixed exchange rate. I this case, sacrificing policy autonomy contributed stability of the exchange rate under the free capital movement[4] However, when they confronted with recession after the First World War, development of interest rate policy to prevent capital flight to the high interest rate America prevented them from taking necessary expansionist policy, and as a result, fixed rate was abandoned[5]. In addition, with the worsening of the World Depression, some countries like UK and France protected their economy by making trade block or monetary area with their colonies.

Taking the experience before the war in mind, the architecture of post-war world economy had to resolve following questions. In the newly created international economy, it must necessary to restrict capital movement, to aim at multilateralism not bilateralism or discrimination, and to assure policy autonomy of the countries. The so called “Bretton Woods system” supported by the IMF, the GATT, and the IBRD created after the war was assumed to contribute this purpose. The aims of the IMF and the GATT was to bring about multilateralism in trade and payments, but the IMF admitted to maintain controls on movement of capital, and it set the mechanism which support national policy autonomy while pursuing external liberalisation . Thus, post-war international world in the Bretton Woods era was constructed to sacrificed capital movement in support of fixed rate and national policy autonomy.

In the field of the International Political Economy, this international framework by the Bretton Woods which enables countries to pursue both external liberalisation and domestic policy goals are called “embedded liberalism” by John Ruggie[6]. Although, the concepts of “embedded liberalism” itself comes from Karl Polanyi’s description on the gold standard, nor Ruggie himself disregarded monetary affairs in his article, most of the modern works dealing “embedded liberalism” framework after Ruggie’s article of 1983 concentrated on its practice in the trade affaires, and

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3 Schenk, Catharine, *International Economic Relations Since 1945*, London, 2011, pp.6-7

4 *Ibid.*

5 *Ibid.*

6 Ruggie, John, ‘International Regimes, Transactions and Change’ in *International Organization*, 36(2), 1983, pp.379-405.

application of this framework to the monetary fields is not fully developed[7]. Thus, before analysing the practice of the "embedded liberalism" to the modern world, it is useful to look back what Polanyi said at first.

According to Polanyi, fundamental transformation of the notion of the policy-makers reflecting the change in society after the World War II occurred, and this transformation of the policy environment made the maintenance of fixed exchange rate more complicated one[8]. Under the classic gold standard, it is natural to take every measure to defend currency, however, in the 20th century, the situation changed. With the emergence of new force like labour party and trade union, and widening of the voting right, budget and monetary policy now became political affairs too. Transition from 19 century classic liberalism to 20th century embedded liberalism made monetary policy secondary issue[9]

One example of adoption of "embedded liberalism" to the international monetary system in post-war era is the work by Barry Eichengreen, and Eric Helleiner adopts the framework to the analysis of Southern countries. Eichengreen have employed "embedded liberalism" framework to describe the transition of the monetary system from 19th century to 20th century.

One of the Eichengreen's theme was to clear whether current tendency to floating rate and monetary union point to ways of reconciling freedom and stability, pointing similarity of gold standard and today, in that both are confronting the conflict between democracy and economic liberalisation[10]. Then, in the last chapter, he concludes that the conflict between capital movement, democracy, and fixed but flexible exchange rate was not solved even by floating the rate but rather abandoned it among the euro members, and it is not to be known if Euro participants will meet what required by "embedded liberalism"[11].

Eichengreen's work looks at broad framework and dynamism of the international monetary system after the war. However, then, how is the practice of the "embedded liberalism" in certain period or certain region? Helleiner tries to show how "embedded liberalism" was implemented in Southern countries after the Second World War. According to Helleiner, Southern countries in post-war era abandoned orthodox approach to the monetary affairs such as central banks with liberal philosophy, or currency boards. Instead, they introduced "embedded liberal" approach to the domestic monetary policy like capital controls, more rigorous pursuit of national goals of development and nation-building[12].

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7 For example, in his edited work of 2008, four of eight articles were trade topics, and no one discuss from the point of view of monetary system, except that of Jacqueline Best who argues how the IMF get rid of Keynesian norms. Ruggie, John (eds.), *Embedding Global market: an enduring challenge*, Hampshire, 2008, Best, Jacquline, 'Hollowing out Keynesian Norms: How the Search for a Technical Fix Undermined the Bretton Woods Regime' in Ruggie (ed.), *ibid.*

8 Polanyi, Karl, *The Great Transformation 3rd edition*, New York, 1962, pp.133-34.

9 Eichengreen, *Globalising Capital* 2nd edition, Princeton, 2008, p.3.

10 *Ibid.*

11 *Ibid.*, p. 232.

12 Helleiner, Eric 'The Southern side of "embedded liberalism": America's unorthodox

Contrasting to Southern example, in the case of Western Europe, “embedded liberalism” under the Bretton Woods system soon proved to be ineffective, and policy-makers began to search for new framework to balance external goal and national goal by pursuing more liberal, market-oriented policy. Although, actual abandonment of the Keynesian policy by Western European countries started from 1980’s, in the 1950’s there had already been policy-makers or intellectuals who found advantage in more “liberalist” policy, although, the content of the “liberalism” had variety of meanings and defers from country to country[13]. Those peoples see’s Bretton Woods system ineffective, and looked for more liberal way to solve the problem facing them.

This is the issue we will look at. In Britain, although the policy management by the Labour government which took power immediately after the war was occupied with domestic concern, such as transition from the war to peace, and welfare state, and used controls and budget as main policy tool while cheap money policy was continued in the monetary field, when the Conservative took office in 1951, some quarter in the government began to contemplate policies relying more on market-oriented solution, insisting on floating rate of exchange, convertibility of sterling, and more active role of interest rate. Reactions of continental Europeans to the British proposal of sterling convertibility and floating rate varied. There was same recognition of ineffectiveness of the IMF framework among the Europeans, for them external liberalisation must be achieved through the OEEC and the EPU progressively.

0.2 British Proposal of floating rate of exchange, convertibility of sterling

Although the international framework itself was ideal, in the actual course of history, stable exchange rate and high economic growth in the golden era of the Bretton Woods system were only short period, and especially early in the early post-war years, the Bretton Woods did not operate well. If so, how did the countries tried to overcome the balance of payments crisis in the inability of the Bretton Woods?

In the 1940’s, immediately after the war, when the UK faced balance of payments crisis, they reacted by restriction of import, strengthening of the Exchange Control Act, devaluation of sterling, and financial aid from the US also help relief the British problems. However, in the 1950’s, this way of handling the balance of payments crisis regarded as insufficient and have only temporal effect, and some of the policy-makers felt the necessity to reform both British economic structure and Bretton Woods system.

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money doctoring during the early post-1945 years”, in Flandreau, Marc (ed.), *Money Doctors: The experience of international financial advising 1850-2000*, New York, 2003, p.249.

13 Articles in Yasuo, Gonjo, *Shinjiyusyugi to Sengo Sihonshugi (Neo-liberalism and Post-war Capitalism), nihon keizai hyoronshya,* 2006, are interesting works dealing the concept of “neo-liberalism” which is not necessarily the same as that of Anglo-Saxon style in continental Europe and the United States, the activities of “neo-liberalist” from the 1930’ to the 1970’s.

"Operation Robot" was such proposal to react the balance of payments crisis started from autumn of 1951 to early 1952 not by conventional measures of tightening of controls, rather it aimed to overcome the crisis by adopting floating rate of exchange and sterling convertibility. The plan was, in a sense, an approach to the IMF objective of liberalisation of exchange control in current account, but breached the IMF rule of fixed rate regime of exchange[14]. In spite of the majority view in the Cabinet that the measure to be taken must be import control and budget cutting, treasury officials though that radical reduction of government spending were, in effect, politically hard , and consequently, British industries lost competitiveness. Thus, they proposed "Operation Robot" to solve the balance of payments problem by introducing market forces, which would settle the exchange rate at appropriate level, stabilize balance of payments, and improve competitiveness. Adding to the concern to the competitiveness by Treasury was the Bank of England's hope to re-establish sterling as an international currency[15]. Although, the "Operation Robot" failed because of the strong objection from Cabinet Ministers except the Chancellor, the next convertibility plan soon got approval in the Cabinet. This time the plan was "Collective Approach to the Convertibility".

"Collective Approach" was a plan which called for cooperation with Commonwealth, America, and Europe in resuming convertibility. In this period, the Europeans too recognised inability of the Bretton Woods system, and some of the Europeans like governor of Bank of France evidently support British plan. Nevertheless, the British proposal did not get support from most of the Europeans, for they support the OEEC and the EPU framework rather than "Collective Approach" as an alternative to the IMF.

Successive British plans were failed, but the British plans posed the Europeans fundamental question of what kind of international framework was appropriate to achieve both external obligation and domestic policy goads.

Existing works on "Operation Robot" and "Collective Approach" were centred on its adequacy as a measure to tackle the problem of the British balance of payments and competitiveness[16]. In addition to the argument on domestic front, Burnham tried to focus its meaning to international economic system, reflecting his International Political Economic interests[17]. But, though his work levels details of the policy-making process, it's description about European reactions are only partial, lacking common recognition to the Bretton Woods by Europeans, and as to the Bretton Woods problem, he explains features and problems in international economy in the 1950's, he did not fully linked the problem under the IMF and British economic policy management, nor did explained the meaning of the EPU and the OEEC in relations to dormant Bretton Woods system.

Therefore, in this discussion paper, I will try to clear in what was the "inability" of the Bretton

14 National Archives, UK: T236/3240, External Action, February, 1952.

15 Schenk, Catherine, *The Decline of Sterling: Managing the Retreat of an International Currency, 1945-1992*, Cambridge, 2010, p. 104.

16 Argument on this issue, see Schenk, *ibid*, pp.105-107, Burnham, *Remaking the Postwar World Economy: Robot and British Policy in the 1950's*, 2003, pp.183-185.

17 Burnham, *ibid.,* pp.175-179.

Woods, and what problem Britain faced because of that inefficiency and Keynesian management of the economic policy, then, look at the policy-making process of "Operation Robot" and "Collective Approach", reactions from Europeans

1. Building of the Post-war Economic system and its Reality

1.1 Pre-supposed Function of the IMF and its Reality

Post-war international economic framework, Bretton Woods system originated from the discussion between Britain and America. Reflecting on the experience before the war, in the negotiation between the UK and the USA, bilateralism and protectionism were ruled out, and progress towards the achievement of multilateral trade and finance was promised. The institutions which set out rules for that purpose were IMF and GATT. In the Bretton Woods system, while signatories were promised external liberalisation, they left rooms for domestic policy. While IMF article 8 ruled the abolition of exchange control concerning the settlement in current account, liberalisation of capital movement was not imposed as an obligation. As to the exchange rate, under the IMF, member countries must commit to the fixed rate of exchange, they are free to change the parity under the consultation with the IMF. In addition, IMF would provide credit to the countries whose balance of payments are recognised as fundamental disequilibrium. Lastly, as already noted, article 8 ruled the abolition of exchange control, article 14 admitted the continuation of exchange control in post-war transitional period which was supposed to be five years.

The system reflected British insistence. On the course of discussion, the US emphasised importance of liberalisation and multilateralism, the British thought dash to liberalisation of trade and payments dangerous, though in discussion on "Robot" and "Collective Approach" in the early 1950'S, the UK insisted on dash to convertibility and the US supported gradually approach to the convertibility. Under the gold standard, if a deficit country tries to resume equilibrium, it must be done by devaluation of its currency or deflationary internal measures. After the First World War, British policy of high interest-rate policy to keep sterling expensive brought about massive unemployment at home. In addition to the painful memory of inter-war period, the British government had promised to realise full employment and welfare states after the Second World War. However, in spite of the promise of full employment, the war-time estimates had already expected huge balance of payments deficits of Britain. Adding up to the balance of payments problem, was mounting amount of sterling liability during the war. Taking all these problems, external liberalisation immediately after the war was dangerous for the UK, and Britain required a mechanism which assured not only external liberalisation but also domestic policy goals be incorporated in the post-war international economic system.

Although the Bretton woods were systematically assured both external liberalisation and domestic goal, in the post-war reality, was that dual purpose be achieved by each country without difficulty? Stephen Gill describes the practice of "embedded liberalism" that notions of the domestic 'mixed economy' and liberalising international economy were, at the time, "relatively compatible”.[18].

But, this description did not correctly grasp the historical fact. Yes, it is true that in the Bretton Woods ear, western countries achieved high economic growth and liberalisation of trade and finance. However, such a golden period of the system existed only limited period, from 1959 after the western countries resumed convertibility of non-resident to the 1968.[19]. The article 14 of the IMF which permits exceptional exchange control during the post-war transitional period continued far beyond five years, and exchange control in current account remained until 1958 convertibility of European currencies. Adjustment of parity did not used as often as expected except the 1949 devaluation of European currencies. IMF credit facilities did not operate because of the lack of IMF resource for the early period. Rather than IMF credit, bilateral credit from the USA played an important role in the balance of payments crisis. Also, in Europe, Bank for international Settlement and European Payments Union acted more effectively than the IMF. After 1959, the system was relatively stable, but after 1968, again, the system turned to be unstable by sterling and dollar crisis, and stagflation in Europe. The Bretton Woods finally collapsed in the early 1970’s[20].

Thus, regardless of the fact that the Bretton Woods system was structured to assure external liberalisation and domestic policy goals, in reality, that compatibility were not achieved in most of the period.

1.2 Balance of Payments Crisis under the Labour Government

Britain after the war was cautious for immediate recession following the inflation, and continued to employ cheap money policy from the pre-war years[21]. As a result, the Bank rate aimed domestic purpose rather than to maintain value of sterling or disinflation.

Since the UK could not depend on monetary policy to prevent outflows of gold and dollars originated from balance of payments crisis, the UK had signed bilateral trade and payments agreement with the European countries since 1944, and import control or suspension of import was ordinary tool when the balance of payments crises occur.

Balance of payments perspective was worse. In addition to the necessity to increase export, there was a problem of sterling liability owed by the UK and scarce gold and dollar reserves which complicated the balance of payments problem more. From the 1945 onwards, amount of the Sterling liabilities had been exceeded the amount of gold and dollar reserves. Consequently, sterling convertibility was continued to be suspended even after the war. Otherwise, call for the

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18 Gill, Stephen, *American Hegemony and the Trilateral Commission*, University of Chicago, 1990, p.96.

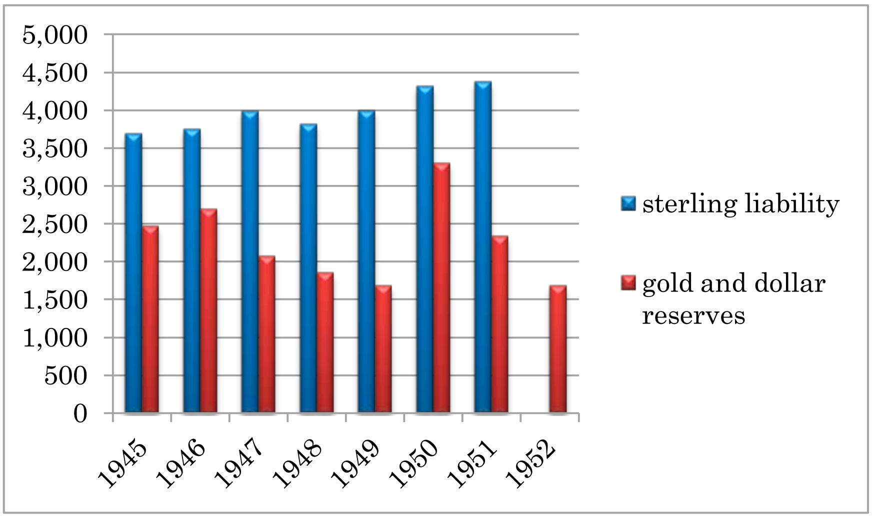
19 Bordo, Michael, D., "The Bretton Woods International Monetary System: A Historical Overview" in Bordo, Michael, Eichengreen, Barry J (eds), *Retrospective on the Bretton Woods System: Lessons for International Monetary Reform (National Bureau of Economic Research Project Report)*, University of Chicago, 1993, p.4.

20 Toniolo, Gianni, *Central Banking Cooperation at the Bank for International Settlements, 1930-1973*, Cambridge, 2005, p.350.

21 Dow, J.C.W., *The Management of the British Economy 1945-60*, Cambridge, 1964, p.14.

repayment of the debt in dollar reserves which was in short both in UK and in the world would press on to the UK .

Figure1: Amounts of Sterling liabilities in relation to gold/dollar reserves (million pounds)



Source：HMSO, *Annual Abstract of Statistics 1938-1951,* p.265.

As predicted in the war-wartime, Britain faced heavy balance of payments deficit after the Second World War, and a progress towards multilateral liberalisation of trade and payments were delayed. Soon after the end of the war, the Anglo-American Financial Agreement was signed in 6 December, 1945 to provide the British the credit of 3750 million dollars, though the sum was not enough to cover all the deficits of the UK. What was more, the British had to promise to resume convertibility of the sterling- the action was thought to be premature- by 1947 in exchange for the dollar. As promised in the agreement, the convertibility of sterling in the current account of non-residents was established gradually from 1947, however, huge dollar drain was occurred as predicted, suspending convertibility again on 20 August. In October, the Exchange Control Act was strengthened further[22]. Now, non-resident holders of sterling were divided into four categories: American Account (freely transferable inside outside the Account), Scheduled Territory (Sterling Area) (Free transfer only inside the area), Transferable Account (freely transferable to Sterling Area, and inside the Account), Bilateral Account (transfer inside the Area required British permission, though administrative transfers were given in many cases. Transfer to Sterling Area was free)[23].

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22 Recent work on why the British signed the disadvantageous agreement like this, seeYuichi Kanai, 'The Anglo-American Financial Agreement and the Crisis of Sterling Convertibility in 1947'　in *Economic Science",* Vol.57, No.4, 2010, pp.54～66 (金井雄一「英米金融協定と 1947 年ポンド交換性回復の挫折」『経済科学』第 57 巻第 4 号』、名古屋大学大学院経済学研究科).

23 Bank for International Settlement*, Annual Report,* 1951, p.140.

After the suspension of sterling convertibility in 1947, British current account tended to stabilize by the beginning of the Marshall, however, from 1949, the balance of payments prospective once again worsened, being affected by the American recession whose consequences were the worsening of the Sterling Area balance of payments and the aggravation of the dollar drain. This time, sterling was devalued, followed by the devaluation of other European currencies like French franc. Since the sterling rate of $4.03 was continuation from pre-war rate, fundamental revision of the rate was needed even there had not been a balance of payments crisis. In 1948, the issue had picked up by Ernest Rowe-Dutton, an official of Overseas Finance Division of Treasury, Robert Hall, and Bolton. In the discussion, Rowe-Dutton insisted on letting the sterling float, but floating was not an option for the Bank in this time, since the Bank thought floating not logical, and must be a last resort, though some of the policy-makers were positive about floating[24].

In the 1949, then Britain faced balance of payment crisis, the focal point was whether to devalue sterling or not, floating was not a choice. Those who favoured devaluation – Clarke, Rowan of Overseas Finance Division of Treasury, later involved in the making of "Operation Robot" and "Collective Approach" – thought that deflationary measures must be accompanied, otherwise, devaluation would be ineffective[25]. On the other hand, those who opposed devaluation – officials in the Economic Section like Robert Hall, Wilson Smith, and Eady – was uncertain about the effect of the deflationary measures, and argued that they were opposed to devalue sterling immediately for it did not take effect without accompanying deflationary measure whose effectiveness was not certain. The view of the Governor of the Bank of England, Cobbold was against sterling devaluation at that time, nevertheless, his view had in common with those of Treasury officials in that both emphasised the necessity of deflationary policy, inclusion of tight money policy in the deflationary measures, and regarded the published government budget cutting in July not large enough[26]. Cobbold's opposition to the devaluation also stem from his desire to foster sterling convertibility as early as possible, and he pointed out three problems to be solved before taking any action on the change of the exchange rate: (a) cost structure, (b) sterling holdings of non-residents, (c) agreement with the USA and Canada- all of these factors would thought to be as crucial in the discussion leading up to "Operation Robot"[27]. Sterling was devalued 30% from $4.03to $2.80 in September 1949 after consultation with the United States and Canada. After the devaluation, the balance of payments recovered, and in 1950, the UK's balance of payments became surplus, but that was only temporary, and the crisis would repeat again in 1951.

Thus, in the 1940's, still in the period of reconstruction, the balance of payments crisis repeated, and since the monetary measures were directed to internal purposes, external liberalisation was impossible, and sterling was totally at the mercy of the crisis. In 1949, sterling was finally devalued, but this was exceptional case, and IMF's adjustable peg was not used frequently. For Britain whose

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24 Howson, Susan, *British Monetary Policy , 1945-51,* New York, 1993, p.240.
25 *Ibid.*, p.245.
26 *Ibid,,* p.246. Cairncross, Alec and Eichengreen, Barry, *Sterling in Decline 2nd edition*, 2003, New York, pp.122-123.
27 *Ibid.,* p.245.

currency was international, devaluation was a last resort.

1.3 Regional approach to the multilateralism – OEEC and EPU

The cause of the balance of payments crisis and dollar problem could be attributed to many factors, but deficiency of the IMF could be one of them. As many argues, “For the first decade of its existence, the IMF played a largely subdued and quite peripheral role in international economic relations. By the mid-1950s, many thought that it had no longer had any significant function and that it should be allowed to fade away quickly”[28]. According to Eichengreen, most of the help to the balance of the payments problem comes from the United States, not from the IMF, and in this period, OEEC, EPU, and BIS contributed more than the IMF[29].

The Americans had to help the balance of payments problems of Europe in place of the IMF, for as long as balance of payments deficit continues, the US ideal of a world of multilateral trade and payments could not be attained, and the US would suffer from trade discrimination by the European countries. Since the desire of the American government was the opening and liberalisation of European markets as soon as possible, at first, they provided the dollar bilaterally to the UK by the Anglo-American Financial Agreement, to France by Blum-Byrnes Agreement, then, multilaterally to Europe, by the European Recovery Programme. Under the Marshall Plan, it was not the Americans who decided the sum of the dollar provide, but the European countries were requested to make a estimates necessary for the recovery by themselves, and under the ERP, the Organisation for European Economic Cooperation was created as an European agency of the ERP, and to promote intra-European trade liberalisation. The OEEC Trade liberalisation Scheme started from 1950. OEEC’s approach to liberalise trade was those which aim to abolish quantitative restrictions between member countries stage by stage.

The European Payments Union was, then, established in September 1950 as a sub-organisation of the OEEC, and its aim was to promote multilateral offsets and payments between the member countries. Before the establishment of the EPU, European trade and finance was dominated by bilateral agreement to economise gold and dollar payments in trade. However, this makes European trade and finance complicated. In the EPU, existing bilateral agreements were all abolished, instead, all the payments between the member countries was gathered to EPU, the payments were multilaterally offset, and only sum of net deficit or credit were paid or received. The payments to the EPU by the deficit countries was settled according to seize of deficits to overall quotas, and the gold payments occurred only at last stage. The EPU also functioned as a financial supporter to the deficit countries providing credit facilities if the Managing Board admitted.

In spite of the fact that the OEEC and the EPU did not promote removal of the trade discrimination to the US, rather it temporary admitted discrimination to the United States, the US regarded the existence of the OEEC and the EPU an essential to the multilateral liberalisation of

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[28] James, Harold, ‘Who owns “ownership”?: IMF and policy advice” in Marc Flandreau, *Money Doctors: The experience of international financial advising 1850-2000*, New York, 2003, p.80

[29] Bordo, Michael D., *op.cit.,* p.45.

Western World. What convinced the US policy-makers the importance of the regional framework was the British experience of the suspension of sterling convertibility in 1947. Too early and too heavy pressure of liberalisation or multilateralism was only to damage the European economies. This was why the Americans had to admit existence of the OEEC and EPU as necessary even though it meant continuation of discrimination the dollar area.

In the negotiation setting up to the EPU, the UK opposed strongly to join the EPU. For the British, existing bilateral agreements were more useful to save gold and dollar payments, and proposed "unite of account" in the EPU might deprive the role of sterling as an international currency at least in Europe. The UK was finally decided to participate in the EPU after achieved US assurance of dollar aide for UK, however, the UK's, or more precisely, the Bank's negligence to the importance of EPU would be continued even after the participation – which we could see in the discussion in "Operation Robot".

2. The search for a new way out

2.1 Balance of Payments crisis and "Operation Robot"

From the early 1951, British balance of payments was again turned to be deficit, and the balance of the whole of the Sterling Area also got into deficit. Foreign reserves, which was ￡3867 million in the second quarter was reduced to ￡2335 million at the end of the 1951, moreover, in the first quarter of the 1952, it became only ￡1500million. Of course, the balance of payments surplus from 1950 disappeared, and show balance of payments deficits 1951 onward. What was worse was the decision of the United States to end the Marshall Plan in 1952, and large reduction of the bilateral dollar support to the UK in 1951.

Table 2: Gold and Dollar Reserves

	March, 1950	**June**	**March, 1951**	**June**	**September**	**December**	**March, 1952**	**June**
(￡millions)	1,984	2,422	3,758	3,867	3,269	2,335	1,700	1,685

Source; HMSO, *Annual Abstract of Statistics 1938-1952,* London, p.265.

Table 3: Current Account of the UK 1946-1951

	1946	1947	1948	1949	1950	1951
Total	-344	-545	-26	5	244	-521
Visible trade	-176	-425	-203	-154	-147	-789
invisible	-168	-120	177	159	391	268

Source：HMSO, *Annual Abstract of Statistics 1938-1952,*London, p.260.

Under these balance of payments crises, Conservative Government led by Winston Churchill took office. Criticising Labour government's policy of high government expenditure contributing to inflationary pressure, it called for more balanced budget, and to avoid inflation, emphasised the necessity to activate monetary policy as an economic policy instrument in the 1951 budget[30]. Insistence on the resumption of monetary policy called back the influence of the Bank of England to the policy-making. Reflecting these change of philosophy of economic policy, its reaction to the balance of payments crisis were totally different from that of the former government.

To the balance of payments crisis started from the autumn of 1951, the government at first suspended the liberalisation quantitative restrictions to the OEEC countries, but it was regarded as not enough, and in the Commonwealth Economic Conference held between 15 January 1952 to 21 January 1952, more drastic steps to improve the situation was called by the participating countries[31]. The Chancellor of the Exchequer, R. A. Butler insisted at the Conference that not only direct measure to reduce balance of payments deficits like import restriction, but also internal measures were necessary, and Commonwealth countries must also reduce the imports from the dollar area to stabilise balance of payments of the Sterling Area as a whole. For his recognition, this conference was the last chance to decide the way to secure the sterling[32]. Despite the Chancellor's emphasis on the necessity of the measures from all aspects, a representative from Australia expressed his discontents with British approach to the crisis. He instead asked the British to take more drastic measures to the sterling problem, if they intended to re-establish sterling strong currency as before, saying that it was not enough to reduce imports from non-sterling area.[33]. What the Australian thought necessary was the convertibility of the sterling to recover the confidence in sterling, and to stimulate investment to the Sterling Area.

Reflecting the results of the Conference, the Chancellor had requested their officials in the External Financial Division to examine the necessary emergency action, and the task was undertaken by Second-Secretary Leslie Rowan, and Under-Secretary R.W.B. (Otto) Clarke both from External Financial Division of the Treasury in collaboration with the Governor of the Bank of

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30 Dow, *op.cit,* p.67.

31 NA: T236/3067, FM(52)1st meeting, meeting of Commonwealth Finance Ministers, 15th January, 1951.

32 *Ibid.*

33 *Ibid.*

England, Cameron Cobbold, and Executive Director, Gorge Bolton[34].

The proposal finally agreed among them was called "External Sterling Plan", or "Operation Robot". The four essences of the proposal were: (a) adoption of the floating rate of exchange, (b) convertibility of sterling, (c) freezing and funding of the sterling balances held by non-residents, (d) re-opening of the London Gold Market.

While the Treasury officials and the Bank were in accordance with the necessity of the sterling convertibility to overcome the situation, their intentions to support the convertibility were different, and their opinions were also different about the issue on floating exchange rate. Whereas the Treasury was more concerned about the deadlock of the economic policy management and lack of competitiveness of Britain rather than the status of the sterling as an international currency, the intention of the Bank was to secure the wider use of sterling as an international currency.

As the domestic economic goal of Britain after the World War II was based on realisation of full employment and welfare state, it was political very difficult to greatly cut the spending on welfare, housing, food subsidies. Reduction of military spending too was impossible if Britain hope to remain the Great Power. All these factors contributed to the inflationary budget deficit. In the crisis of 1949, sterling was finally devalued after controversial discussions in both domestic and external front, in the crisis of 1951-52, the devaluation was excluded from the option, because "no-one would believe that this devaluation following only 30 months after the last, was the final one", "foreigners would take such a devaluation as a confirmation that sterling was going the same way as the French franc"[35].

Other measures like another reinforcement of quantitative restriction to the OEEC country's export would mean retreat from the liberalisation of trade, especially because the UK had already did so. In addition, while IMF did not fully work in this period and the only reliable source of credit to Britain in the event of balance of payments crisis was the United States, unfortunately, the European Recovery Programme would planned to be terminated in 1952. On the other hand, even if Britain fortunately could obtain another financial support from the US, that could not resolve fundamental problem of the British economy. The cause of the problem, as discussed by Clarke of Treasury and the officials of the US in this era, was lack of competitiveness of the British industry. The effect of American aid would only delay the necessary economic reform in Britain.

Floating rate and Convertibility by the Robot were a measure to provide market mechanism which would bring about efficiency and competitiveness to the British economy. Clarke though that as long as the UK remained fixed rate of exchange, she would lose large amounts of gold and dollar reserves each time the crisis occurs, but contrary to the fixed rate, under the floating rate, the rate of exchange would take the strain, not the reserves[36]. In addition, he expected that the sterling would be fallen after the adoption of the floating rate, and that would promote export and reduce imports, thus improve balance of payments. However, the most important reason for him to support floating

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34 The name "Robot" was a code name taking from the initials of *Ro*wan, *Bo*lton, *Ot*to Clarke.

35 NA: T236/3240, External Action, 1952.

36 *Ibid.*

rate was that while the painful processes of higher cost of living and unemployment was inevitable during transitional period, which would force uncompetitive British industries to restructure its industries in the long run[37]. Secondly, since the reason of the suspension of the sterling after the war was a lack of gold and dollar reserves, if the problem of scarce reserve would disappear or at least became minor problem by introducing floating rate, the reason to suspend the convertibility would also disappear..

Thus, the attitude of the Overseas Finance Division was that the key to approach the British difficulty was to reform British economy, and the decrease of the value of sterling as an international currency as a result was unfortunate but inescapable for that purpose. To the contrary, the Bank's intention of the Robot was to re-establish sterling as an international currency.

Under the Labour party, the Bank of England was nationalised, and interest rate had been kept low for the purpose of economic reconstruction and to avoid recession, consequently, the Bank's role in the making of monetary policy was very limited one. After the change of the government from Attlee's Labour to Churchill's Conservative in the October 1951, the Bank had started to promote more active use of Bank Rate as a policy tool, and had open the London Foreign Exchange Market in December 1951t with more flexibility to exchange rate[38].

A problem which bothered the Bank who aimed to resume sterling as an international currency was "cheap sterling". From the late 1940's, in the free exchange markets outside the UK like New York, Zurich, Transferable sterling was unofficially exchanged with the dollars at the rate cheaper than official sterling-dollar exchange rate of $2.80[39]. The sterling exchanged at free market was called "cheap sterling", and it brought about some disadvantages to the UK.

The "cheap sterling" dealing were, according Bolton, comparatively new phenomena which could not be assumed in the early 1940's when the most of the trade was under the government hands[40]. However, with the increase of private trade, various technics like "cheap sterling" developed. In this new situation, suspension of sterling convertibility would only to bring about disadvantages to the UK. Since the Bank of England's exchange control was effective only to the resident of the UK, continuance of the suspension of sterling convertibility would exclude British merchant from international dealings. Even by strengthening the exchange control, it would make sterling more and more unacceptable as an international currency. Further, the unofficial dealing like cheap sterling means loss of dollar earnings, and, reveals the fact that the Bank of England could not manage or control their own currency thus losing the confidence to the pound more and more[41]. To solve this cheap sterling problem, convertibility of sterling was crucial, for if the arbitrage of the sterling occurs from the existences and differences of both the official rate and transferable account rate, this arbitrage would disappear once sterling recover the convertibility,

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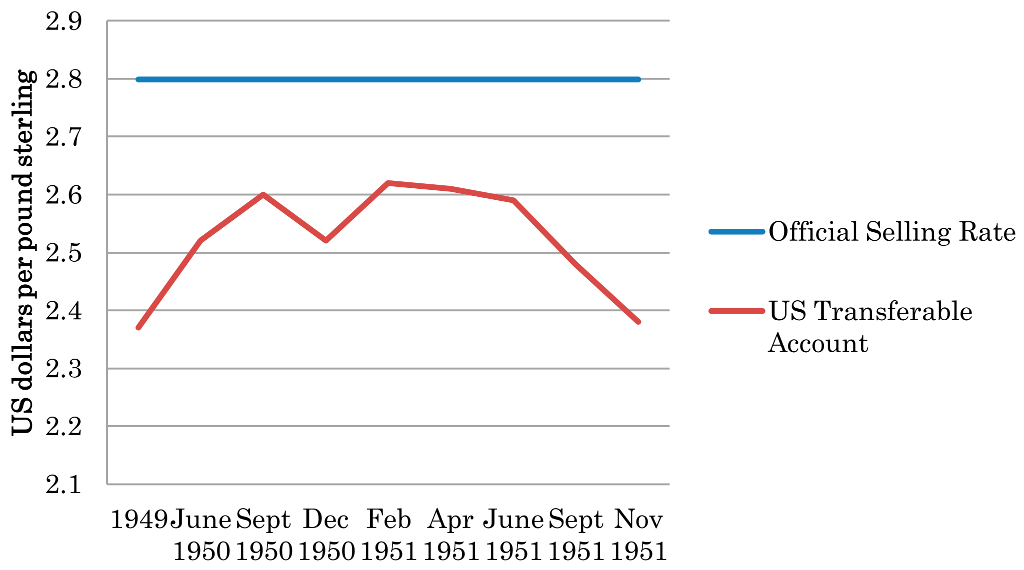
37 NA: T236/3240, R.W.B.Clarke to Leslie Rowan, 25 January, 1952.
38 Fford, John, *The Bank of England and Public Policy 1941-1958*, Cambridge, 1992, pp.412-416.
39 Ways of cheap sterling dealings, and its genesis, see, Fford, *ibid*, pp.223-225.
40 NA: T236/3240, Inconvertible Sterling, 16 February, 1952.
41 NA: T236/3240, R.W.B. Clarke to Leslie Rowan, 25 January, 1952.

integrating the two rates into one.

Thus, although the intentions of the Treasury officials and the Bank differed, both found some advantage in establishing convertibility in this period.

Figure2: Transferable Sterling Rate and Official Rate



Source: International Monetary Fund, *International Financial Statistics*, Washington.

2.2 The deficiencies of Robot Plan

When the Chancellor Butler presented the plan to the Cabinet in February, the proposal contained four points: flexible rate, sterling convertibility, freezing of a part of the sterling balances, reopening of the London gold market. But the Robot did not appeal the Cabinet ministers, for the plan had some defects both domestically and externally.

At first, although Clarke regards floating rate convertibility as a remedy to bring about structural reform in British economy, that would be brought about only after a long transitional period; for the short-term, the result would be rise of import prices and living standard, damaging the industries and increasing unemployment[42]. In addition, contrary to the presumption of the Robot support's thinking that the fall of the exchange rate as a result of the floating would increase the exports, and then, improve the balance of payments, the critics like Lord Cherwell of the Paymaster-General had completely opposite opinion that the root of the problem was not a high cost structure of the British industry, but the shortage of the supply of materials like steel and labour in the industries[43].As a result, it would be impossible to increase the exports merely by adopting the floating rate.

The second problem of the Robot was concerned with the trade liberalisation scheme in OEEC. Robert Hall, a chief of the Economic Section of the Cabinet Office, and Edwin Plowden, an

42 NA: T236/3240, External Action

43 NA: T236/3240, The Balance of Payments, Paymaster General.

influential member of Economic Planning Board, feared that the unilateral British action of the sterling convertibility would cause downward spiral of the European trade. The reason is that if sterling resume its convertibility independently, it is natural to think that other soft currency countries in the OEEC would seek to earn sterling so as to convert sterling to dollar later, but this would be done by increasing exports to the UK, and strengthening quantitative restriction to the exports from Britain[44].If British reaction to these measures by soft-currency countries would be retaliating imposition of the quantitative restrictions, the OEEC would become an arena of not trade liberalisation but trade war[45]. Moreover, Hall estimated that the strengthening of the quantitative restrictions on British imports would increase unemployment of more than 100,000 people. From the above reasons, Hall concluded in his memorandum that the implementation of the Robot meant abandonment of the British objectives of achieving full employment and high level of trade, and Britain should search for another way to tackle the balance of payments problems[46].

The two reasons were plausible enough for the ministers to refuse the Robot. However, the Robot was external difficulties too– its effect on the EPU, Sterling Area, and in relation to the existing IMF obligations. The assumed effects of the sterling convertibility by the adoption of Robot to the EPU would occur in three aspects: (a) the meanings or reason of the existence of the EPU itself; (b) its impact on the working of the multilateral payments system of the EPU; (c) effects on liberalisation of trade.

As to (a), the EPU was a transitional organisation with an aim to promote liberalisation of payments supporting the liberalisation of trade, and would end its working if the major European currencies established their convertibility, thus, making the existence of the EPU unnecessary[47]. More precisely, it was formally ruled that in the EPU, convertibility of the currencies of the member countries whose total sum of quotas in the EPU exceed more than 50% of the total, would bring about automatic clearance of the Union, and it was recognised in this period that if the sterling recover its convertibility, at least Germany, Belgium, and Holland would be followed – total of the quotas of these countries would be over 50% of the total.

Even if hard-currency countries could manage to stay in the EPU after the convertibility by some way or others, this would cause technical problems in the payments mechanism – this was the point (b) above. If sterling would stay in the EPU after the convertibility, soft currency countries could possibly try to draw credit – convertible sterling – from the UK as much as they could through EPU until the obligation of gold payment occurred.

Finally, as to (c) above, the disappearance of the EPU meant not only the loss of the important organisation to facilitate multilateral payments in Europe, but it would also have negative effects on trade side. One of the features of the EPU was its credit facilities to the debtor countries in Europe, and often supported the countries like France when they got into severe balance of payments crisis,

44 NA: T236/3240, Robert Hall to Edwin Plowden, 22 February, 1952.
45 *Ibid.*
46 NA: T236/3240, Robert Hall to Butler, 25 February, 1952.
47 NA: T230/263, to Robert Hall, Collective Approach in Relation to EPU and Other European Institutions, 13th February, 1953.

for the EPU credit facility were effective in the absence of the presupposed IMF credit. If the credit facility were to be lost, that would make the debtor countries much more difficult than present to promote liberalisation of trade.

Those were the major point as to Robot in regard to the effect in Europe. From the point of the view of the Sterling Area countries and the United States too, Robot was problematical. For the Sterling Area, the freezing of the sterling balance could not be defended and justified, meaning "the banker shutting his doors", and would have devastating effects to the Sterling Area countries like the aggravation of the starvation in poor countries[48]. As to the United States, Robot was, in a way, an approach to the US objective of the multilateralism and convertibility, but in another way, it was a divergence from the US objectives, since it insists abandonment of the fixed rate, and re-opening of the London gold-market without asking any US opinion, although under the IMF, only the US dollar has formal convertibility to the gold on fixed price[49]. Taking all these points in mind, in March 1952, the Cabinet decided not to adopt Robot plan, and decided to tackle the balance of payments problems by import reduction, reduction of military budget, housing budget, and to re-examine investment plan, and it was promised that if the situation would be aggravated again, the Cabinet would reconsider the Robot[50].

The first trial to persuade ministers to adopt sterling convertibility was ended with failure. But the fear for another crisis was not disappeared, and the search for the way out continued.

3 Not "Two-world", but "One-World"

3.1 "Two-world" solutions

While the Budget of March 1952 announced the policy based on the conventional approach, the budget did not remove the fear for the recurrence of the crisis. In addition, since it had been promised at the Commonwealth Conference in January that the British would propose new policy to get rid of the balance of payments crisis at the Commonwealth Prime Minister Conference in autumn of the year, British policy makers continued to search for new plan. From February to March 1952, the plans which formalise the discrimination to the dollar area were proposed by Bolton of the Bank of England, and an official of the Economic Section. However, these plans were far from the "one-world" policy proposed by the Chancellor of the Exchequer Cripps in that time when the country faced the devaluation of the sterling or not in 1949. Rather, both plan – called "two-world" plans – emphasised the necessity of the continuation and strengthening of the discrimination to the dollar area by establishing sterling system in Europe or creating discriminatory economic bloc between Sterling Area and Europe.

In February 1952, George Bolton proposed new trade and payments system with European countries whose trade and payments relations were closely connected with the Sterling Area countries after the realisation of the sterling convertibility. One of the deficiencies of the Robot was

48 NA: T236/3240, note to the Chancellor of the Exchequer, External Action, February, 1952.

49 NA: T236/3240, Plan for "Overseas Sterling", no date.

50 NA: CAB128/40, CC(52) 23rd, 24th and 25th conclusions, 23rd and 29th February, 1952.

the possibility of the down-ward spiral of European trade, by strengthening of the quantitative restrictions to the UK by soft currency countries after the sterling convertibility. Interestingly, Bolton's idea of new sterling system was not the one which tried to avoid the emergence of such trade discrimination between European countries, but his idea assumed that the trade discrimination was unavoidable in the world after the convertibility and tried to establish little sterling system among certain European countries[51].

According to the "Payments Club" of Bolton, Europe could be divided into two Groups after the convertibility. List A (Austria, Germany, Greece, Italy, Spain, Swiss, Turkey) was assumed no to be a participant of the Club since its relations with the Sterling Area or the Commonwealth were not strong. These countries would not be supplied any special sterling facilities by the UK. To the countries of the List B (Denmark, Finland, Sweden, Belgian, France, Holland, Portugal) who had interests in holding sterling, the UK would provide certain benefits in condition that they would participate the new sterling system. For example, the UK and the List B countries would: (a) ratify the trade agreement so as to avoid dollar earning competition each other, leadingto the making of the preferential trade system in the long run. (b) "External sterling" earned by the List B countries were conserved so as to prevent excessive devaluation of the participating countries' currencies. In return, the B countries who need "External Sterling" would benefit from the relaxation of the credit restrictions in the London Market. (c) To finance the countries temporary require the sterling, "External Sterling" would be pooled[52].

Under the Plan, the EPU was supposed to be disappeared with the convertibility of sterling. In that case, (a) the EPU would be cleared on 30th June, the debt of the 15 million pounds by the UK to the EPU would become "Old Sterling" which could be usable to the payments of the debt to the UK[53]. (b) List B countries holding "Old Sterling" in the EPU was given a special facility to convert the "Old Sterling" to "External Sterling" to a certain agreed amounts.

This kind of association with the Sterling Area and Europe was also considered in the Economic Section. An Economic Section official, Robert Nield proposed "Sterling Union" requiring reformation of the existing Sterling Area system and participation of the EPU into the Sterling Area. It assumed the continuance of the inconvertibility and fixed exchange rate system, and proposed (a) to abolish the dollar pool system of the Sterling Area, instead, the dollar earnings of the participating countries were redistributed among them. (b) to eliminate gold payments, abolish automatic payments system of the EPU, and the EPU would participate in the Sterling Area in the future.

By these measures, Nield though that the down-ward spiral of trade could be avoided with a plenty of credit facilities inside the Union[54]. Another merit of the plan was that by not just pooling, but redistributing the dollar, it could give each of the Sterling Area countries responsibility to take measures to maintain foreign reserves and dollar import, enhancing the responsibility. However,

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51 NA: T236/3241, George Bolton, The Plan and Europe, 27th February, 1952.
52 *Ibid.*
53 NA: T236/3241, Bolton, The Plan, 4th revision, 14th March, 1952.
54 NA: T236/3243, External Sterling Plan, 4th April, 1952.

paradoxically, if responsibility of the balance of payments deficit by the each Sterling Area countries enhanced, that would be an incentive for the Sterling Area countries to look for new measures to earn dollars and could finally be brought about shift of exports from UK markets to the US. As regards the EPU, whereas eliminating gold payments from Europe and redistribute dollars among the countries could be regarded as an "every advanced form of European integration", it was that the integration of Europe which the Europeans sought for[55]. Lastly, to avoid competition with the dollar area by establishing discriminative economic block did not resolve the problem of the high cost structure of the British industries, rather it merely prolong the problem.

To these "two-word" approaches, Clarke showed negative attitudes. As we later will see, if the UK plays a central role in any "two-world" system between the Sterling Area and Europe rejecting American involvement, Britain must even more be economically strong enough to support the block. Thus, Clarke pointed out the unreality of the "two-world" course saying that "I would not myself agree with the proposals of the Bank, which seek to incorporate Western Europe in the sterling area. I do not believe that we are strong enough to carry the load which is implicit in such proposals,…", "we must find a new basis for cooperation with Europe"[56]. He also rejected "Sterling Union" by pointing out that by dividing the western world into two, it brought about continuance of the high cost structure inside non-dollar block by avoiding competition with dollar goods[57].

3.2 Atlantic Payments Union

It was not only "two-word" plan which gave more weight to resolve "dollar problem" first rather than rush to the convertibility. Lord Cherwell and MacDougal also thought that the resolution of the "dollar problem" is the first consideration to early realisation of convertibility, and propose the plan of Atlantic Payments Union. The difference of the APU and "two-world" idea of the Economic Section was that the APU intended to include – not exclude – the USA from the plan.

Their idea of APU originated from World Payments Union by the Secretary-General of the OEEC, Robert Marjolin. on which had asked the British government to consider in May, but had rejected by the British[58]. However, different from many of the policy makers, Cherwell and MacDougal was impressed by the Plan, and proposed the establishment of the Atlantic Organisation for Economic Affairs and the Atlantic Payments Union under the AOEA, to the Cabinet Committee lead by Foreign Secretary Anthony Eden in August 1952. Its participants were assumed the Commonwealth countries, the OEEC countries, and the USA and Canada.

The proposed APU was modelled on the EPU mechanism in its multilateral clearance, mutual credit facilities. The difference was that in the APU, settlements with the persistent creditor – evidently the USA – was excluded from the regular settlement in each month, instead, in the settlement with persistent creditor, a system of "gold tax" – imposed on the excess deficit to

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55 *Ibid.*
56 NA: T236/3241, Clarke to Rowan, Robot Walks Again, 11 March, 1952.
57 NA: T236/3243, External Sterling Plan, 4th April, 1952.
58 In detail of Marjolin's plan, see next Chapter.

persistent creditor – and “gold bonus” – receive when in surplus with persistent creditor – would be introduced according to its balance of payments position with persistent creditor, which finally lead to the incentive to equilibrate the balance of payment[59]。 Under the APU, discrimination against the dollar area was permitted.

Since the APU had a possibility to develop the cooperation with the USA and Canada in the field of international economy, Clarke appraised the APU in this regard[60]。 Robert Hall pointed out that the APU covered strategically important areas for the Western camp, and assured that the ambitious plan like this would attract the Americans without fail[61]. Nevertheless, APU was technically and politically difficult .

Firstly, gold tax and gold bonus system, and authorisation of discrimination against dollar zone were too heavy obligation to the USA. Secondly, while the participation to the APU could be a preparation to the currency convertibility resolving the dollar problem, it did not mention each step to the convertibility – in the EPU, the ratio of gold/credit was central issue to reach the convertibility[62]。 Thirdly, contrary to Hall’s appraisal of APU’s importance as a Western Alliance, others pointed out its strategic insufficiency for the APU did not assume participation of the Latin American countries and Japan- - both were important to America[63].

Thompson-MacCausland, an advisor to the Governor of the Bank of England, in this discussion with Brittain, expressed his view on it[64]。According to Thompson-MacCausland, it is of course very good idea to establish a framework in which the USA participate, and discuss about the Balance of Payments regularly, but there do not exist the system of central control of dollars, in addition, the concept of “control” was something to be regarded as “negative” in the USA[65]. From the point of the Sterling Area, under the APU the Sterling Area would be treated as one unit, causing much of the feeling of unfairness and discontent among the Sterling Area countries, for if the Area treated as one, a member country’s dollar credit might be used to offset other members’ deficit[66]。 Since such discontents already exist under the existing unofficial arrangements, under the stricter rule of the APU, their dissatisfaction would mount more. On the other hand, if each members of the Sterling Area would have each account, they had to establish relations with all the central banks of the APU member countries, reducing the use of sterling by the Sterling Area countries. Those were the

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59 NA: T236/3076, PEC(52)17, 1st September, 1952, Atlantic Payments Union, report by a group of officials.

60 NA: T236/3076, FEF to Brittain, Armstrong, Atlantic Payments Union, 5th August, 1952.

61 NA: T236/3076, Robert Hall to Armstrong, Atlantic Payments Union, EPC(52)7, 6th August, 1952.

62 NA: T236/3076, FEF to Brittain, Armstrong, Atlantic Payments Union, 5th August, 1952.

63 *Ibid.*

64 NA: T236/3076, Thompson-MacCausland to Figgures, Paymaster-General’s Memorandum: PEC (529)7, 5th August, 1952.

65 *Ibid.*

66 *Ibid.*

points MacCausland criticised the APU[67].Although, the APU had its attractiveness, it had in many points unrealistic.

3.3" Collective Approach to the Convertibility"

Thus, in the first half of 1952, various plans to overcome the balance of payments problem were raised, but each had its deficiency. British policy making was in confusion. For that reason, for the preparation for the Commonwealth Prime Ministers Conference in autumn 1952, Britain, first of all, have to decide its basic policy line. This task was accomplished by the working party on external economic policy under the Cabinet Committee on Preparations for Commonwealth Economic Conference lead by Eden[68]. The working party on external economic policy raised multilateralism, bilateralism, discriminatory block as a possible option, but denied the last two. As regards bilateralism, it would not contribute to the balance of payments probleme, rather it would make gold and dollar earnings much more difficult, and mean complete retreat from the multilateralism which was the post-war promise at the Bretton Woods[69].

Creation of the discriminatory block did not seen as advantageous too, especially from the point of view of the Sterling Area. Although traditionally, the most important trading partner of the Sterling Area countries were the UK, and the each of the member countries were also important trading partner, they were also highly dependent on the imports of primary products from the outside the Sterling Area. Those products were, wheat, softwood, and metal from Canada, cotton, grains, tobacco, machine from the USA, oil from Venezuela – all of which were not produced in the Sterling Area[70]. Despite this dependency on outside world, making of the discriminatory block would not reduce imports from outside the block. Even if they tried to produce those produce inside the block, it would require huge investment and long time. Therefore, bilateralism and discriminatory trading block was refused as a basic policy line, and the multilateralism was chosen as a future policy line of Britain.

In conclusion of the policy paper, the working party concluded that to bring about multilateralism to the free world, both side – creditor and debtor – must do effort, and emphasised the importance of the cooperation with the USA, Commonwealth and Europe.

Having confirmed that the British long-term policy must be based on multilateralism, the working party submitted the paper to approach the problem multilaterally on the 1st September 1952. In a paper titled "Step Towards Convertibility", the officials emphasised the necessity to resume sterling convertibility as soon as possible, casting doubts on the APU idea.[71]. The paper

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67 *Ibid.*

68 NA: CAB130/78, Gen412/1st meeting, working party on external economic policy, 1st July, 1952.

69 NA: CAB130/78, Gen. 412/4(Final), 16th July, 1952, The problems of External Economic Policy, memorandum by a Group of Officials.

70 *Ibid.*

71 NA: T236/3368, PEC(52)18, Cabinet Committee on Preparations for Commonwealth Economic Conference, Step Towards Convertibility, note by the acting secretary, 1st September, 1953.

began by describing what kind of damage the UK would suffer if the sterling would remain inconvertible. The central point of the convertibility of sterling as an international currency was that although, in case of a currency used only domestically not internationally, only freedom of resident matters, in case of international currency, non-resident must free to use sterling anywhere in the world, both inside and outside UK[72]. If sterling would continue to be inconvertible, (a) international status of sterling would be lost, (b) Cheap sterling would spread, causing damages to the British traders[73]. To avoid this consequence, the paper set out four measures. (a) To create a group of core countries consisted of the UK, the US, Canada, France, Germany, Benelux. Inconvertible countries among the group would establish convertibility on the same footing (b) It is free to choose flexible rate or fixed rate, but the UK would adopt flexible rate. (c) Abolish all trade discrimination to all the core countries except persistent creditor, provided that the rule applies only to quantitative restrictions, and preservation of tariffs and imperial preferences would be admitted. (d) Establish Exchange Support Fund to which the United State would support financially. Assuming that all the necessary procedure by the Congress would be completed between summer and autumn of 1953, the proposed would starts from early 1954[74]。 These four sets of proposals came to be called “Collective Approach to the Convertibility”.

“Robot” and “Collective Approach” were in common in that both involve sterling convertibility and floating rate. However, Why the “Collective Approach” which had similar features with that of Operation Robot could be passed the Cabinet? When the committee on the external policy submit the “Collective Approach” to the ministerial committee, some of the deficiencies of the Robot were overcome, and though the problems of the impact on the domestic economy was left open, the proposal finally achieved supports from the former critics to the Robot - Board of Trade, Foreign Office, Colonial Office, Commonwealth Office.[75]

When Robot was discussed in early 1952, the Foreign Office feared political impact of the Robot plan to Europe, Board of Trade was anxious about contraction of trade by inconvertible countries strengthening quantitative restrictions on UK export to accumulate dollar earnings[76]. On the contrary, “Collective Approach” give more weight on the European cooperation , for it emphasise equal footing with major European countries on convertibility, and it also set out abolition of quantitative restrictions to avoid trade discrimination following the convertibility. Exchange Support Fund had a purpose to support sterling if the rate of sterling excessively fall after adopting flexible exchange rate[77].

However, the elements of “European cooperation” were only to British eyes, for Europeans, this was nothing but an unilateral British proposition disregarding the importance of the existing liberalisation framework and programmes in the EPU and the OEEC.

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72 *Ibid.*
73 *Ibid.*
74 NA: T236/3368, Herbert Brittain to Armstrong, Report of convertibility working party, 1st September, 1953.
75 *Ibid.*
76 *Ibid.*
77 *Ibid.*

4. European Reaction to the "Collective Approach"

4.1 Robert Marjolin and World Payments Union

In January 1953 when the "Collective Approach" was formally announced a the OEEC Council, Hugh Ellis-Rees, a representative of the UK delegation to the OEEC, warned the British government that the Europeans were anxious about the effects of the sterling convertibility to the EPU, and to the OEEC trade liberalisation scheme after the collapse of the EPU[78]. This warning by the Ellis-Rees was corresponded to the severe attitude of the chairman of the OEEC, Robert Marjolin. However, Marjolin at least had same opinion with the UK as regards the ability of the Bretton Woods system to solve the world dollar problem or balance of payments disequilibrium problem. In May 1952, when "Collective Approach" was not even formed, he had proposed World Payments Union to solve the dollar problem.

The World Payments Union reflected the prevailing feeling in the Managing Board of the European Payments Union that the Bretton Woods system was a "failure", and some measure must be found to resume the idea of the Clearing Union proposed by Keynes at the negotiation with the US on post-war international economic framework[79]。 However, in 1952, it was regarded as inappropriate to apply Clearing Union as it was discussed in the 1940's, instead, the EPU could be a substitute for Clearing Union.

In May 1952, when Marjolin visited London, he unofficially revealed the Scheme to the British. He, as a Secretary-General of the OEEC, was interested in "dollar problem" in Europe, and expect that if the next American President would be Dwight Eisenhower, he would propose a scheme which could be a new departure solving the problem of the balance of payments disequilibrium between dollar area and non-dollar area[80]。 In the World Payments Union with EPU type settlement mechanism, western countries could discuss about balance of payments problems and dollar aid with the United States[81]。

In addition to the disappointment with the Bretton Woods, Marjolin thought there were not much room of policy manoeuvre for the British and other European countries, for cutting of investment, housing, defence necessary for the improvement of living standard in Europe were something politically difficult to accomplish drastically[82]. This was why Marjolin reached the conclusion that the only hope was the financial and economic policy of the United states enlightened by Europeans[83].

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78 NA: FO371/105851, Draft Submission to Ministers, OEEC and the Collective Approach to convertibility, attached to 13th January, 1952

79 Historical Archives of the European Union (HAEU), Italy, EPU/EMA33, TFD-232, convertibility and how to get it., 17th May, 1952.

80 NA: T232/343, Robert Hall, note of discussion, 6th May, 1952.

81 *Ibid.*.

82 NA: T232/343, E. A. Berthoud, Monsieur Marjolin's visit to London, 10th May, 1952.

83 *Ibid.*

4.2 Reactions of the European Central Banks and the Governments

In spite of the common thinking on the Bretton woods system, at the informal discussion between Marjolin, British officials, Foreign Secretary, the Chancellor of Exchequer, he showed strongly cautious about the impacts on the OEEC and the EPU by the "Collective Approach". The reason was not only the effects of the "Collective Approach" to Europe, but the British intention to go into discussion with the USA on it before consultation with Europe. Nevertheless Bolton belived that the opposition to the British plan were only fanned by limit circles in Europe[84]. Why Cobbold believed would get support from the Europeans? The reason lies in French experience under the Bretton Woods, and the positive attitude of the governor of the Bank of France to adoption of floating rate in May 1952[85].

The most important objective of the France after the Second World War was the modernisation of the French industry which leads to the inflationary economy and monetary instability. French franc had devalued in January 1948, and established multiple exchange rate system, imposing different exchange rate for hard currency, breaking the cross rate between sterling and the dollar. This breaking of the IMF rule was blow to the IMF prestige[86]. Further, in 1949 before the establishment of the EPU, the French seriously discussed the possibility of the economic area called "Fritalux" or "Finebell" between Benelux countries and Italy under which they intended to adopt liberalisation of capital flows and the floating rate of the exchange. The failure of the plan attributed to the refusal by the United States who preferred the economic integration among larger group of countries which finally lead to the establishment of the EPU to "Pétit Europe". Taking these historical facts into account, it was not surprising if the French welcomed the "Collective Approach" which restructure the IMF and allow floating rate of exchange. However, although the Governor of the Bank of France, Wilfrid Baumgartner, showed interest in successive British proposal informally, it finally turned out to be that the opinion of the Baumgartner as a central banker was not share by the government policy-makers.

When the Chancellor visited Paris on 6 and 7 June 192, from the informal discussion among he and the French Prime Minister, Antoine Pinay, Baumgartner, Guillaume Guindy from French Department of Finance, Cobbold and Rowan of external financial division of the Treasury, he received the impression that the French had strong interests in the adoption of the floating rate of the exchange[87]. However, on the next day, when he had a chance to talk with only Guindy, he told the Chancellor that the possibility of the French suddenly resume the convertibility of franc was

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84 Bank of England Archive (BOE): G1/98, to Deputy Governor, Shiepmann, George Bolton, February, 1953,

85 NA: T236/3244, Anglo-French Exchange Policy, 30th May, 1952

86 Bordo, *op.cit*, p.46. France imposed per value of 214.39 franc for basic imports, but for tourist and financial transactions, adopted a floating rate. For the soft currency, official rate was employed.

87 NA: T236/3244, Record of an informal discussion after lunch with the Governor of the Bank of France on Friday, May 6, 1952. According to a paper lightly before this one, from some evidence ensures that this informal discussion was held on 6 June, not 6 May as noted in the document. Fford also pointed out this error, Fford, *op.cit,* p.458. Antoine Pinay served as Prime Minister from 8 March 1952 to 8 January 1953.

scarce, and what was discussed in France was only a floating rate without commitment to the convertibility[88].

Later in January 1953, after the “Collective Approach” was formally announced to the Europeans, Prime Minster René Mayer also expressed his view that he personally supported the operation of the convertibility, but the operation must not sacrifice neither the EPU nor the OEEC, and it must be important to avoid the collapse in the economic sphere when the Europeans were doing every efforts to promote the integration of Europe by the European Defence Community.[89] In addition to the opinion of the Mayer, Paris report to the American State Department also pointed out that the French were thinking convertibility of the franc only in parallel with the liberalization of trade, and without effective substitute to the EPU, the French could not support the any plans which dismantle the EPU[90]. For France who was a debtor in the EPU, the EPU was an important source of the credit and its existence was vital. Since France was denied access to the IMF resources after the breaking of the IMF rule on cross rate – even though the IMF had not yet played an active role - , the EPU credit was only reliable external source after the termination of the ERP[91]. Therefore, some of the socialist even regard the British plan as a measure to setback the French plans of the European integration.[92].But, in anyway, in spite of early and strong support to the floating rate from the Bank of France, at the government level, the “Collective Approach” was regarded only as a setback to the OEEC liberalisation programme, the EPU, and integration of Europe.

That were the reactions of the debtor country in the EPU, France. Then, what were the view of the Germans and the Belgians – creditors in the EPU – to the convertibility and the “Collective Approach”? At the discussion with the Germans in 12 May, 1953, German officials told the British that since 70% of the total German trade was conducted through the EPU, they had a vital interest in the liberalisation of trade inside Europe, and because this problem had a certain link to the economic and political integration plans, they wished to have a common convertibility plan under the EPU framework[93].

Ludwig Erhard, the Economic Minister, was more or less open in mind, and welcomed the movement to the convertibility by the British and expressed sympathy and interests[94]. To the contrary, Von Mangoldt from the Federal Reserve Bank insisted that the convertibility must be

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88 NA: T236/3244, Record of an informal discussion after lunch with the Governor of the Bank of France on Friday, May 6, 1952, T236/3244, Record of discussion on Saturday, June 7th 1952 in Paris.
89 BOE: G1/98, C.F. Cobbold to Chancellor, 12th, January, 1953, FO371/105851, From Paris to FO, 19th January, 1953. René Mayer served as Prime Minister from 8 January 1953 to 28June 1953.
90 National Archives and Record Administration (NARR): RG469, NND887841, MSA Paris to Secretary of State, January 16, 1953.
91 Bordo, *op.cit.*, p.46.
92 NARR: RG469, NND887841, MSA Paris to Secretary of State, January 16, 1953.
93 NA: T230/263, UK record of meeting in London between UK and German officials, 12th May, 19523.
94 NA: T230/263, UK record of meeting in London between UK and German ministers, 152h May, 1953.

approached through the institution of the EPU, and it must not be a dash to the convertibility.

The reactions of the Belgians were similar to those of the Germans. At the discussion on 15 and 16 May, a representative of the Belgium showed his anxiety that with the convertibility and the distinguish of the EPU, the IMF article 14 became ineffective, and the Europeans must immediately remove quantitative restrictions to the dollar area[95].And like the Germany, insisted the institutional approach to the convertibility through the EPU[96]. This view was reiterated to the Americans when they visited the Washington[97].

Thus, in spite of the mounting interests in the convertibility among the certain Europeans, and the Germans were even welcomed the proposal of the convertibility itself, support for the British approach to the convertibility was minority. On the part of the British, the disappearance of the EPU followed by the convertibility was unfortunate but unavoidable consequences, but on the side of the Europeans, the convertibility must be tackled through the EPU and it should not be a dash to the liberalisation: it should be gradually approached in parallel with the trade liberalisation.

By the June 1953 discussion of the OEEC council, Marjolin even expressed his displeasure to discuss the problem of the convertibility at the meeting of the OEEC[98]. There was no room for the “Collective Approach” to intervene in the minds of the EPU countries.

Conclusion

The UK was involved in the creation of the post-war international economic framework, but the practice to the liberalisation was difficult. Facing the balance of payments crises, import control was often introduced, exchange control was strengthened. Monetary policy was exclusively directed to reconstruction needs, there are no room to manipulate interest rate for the sake of the stability of balance of payments and sterling. In addition to British problem, the role of IMF was limited and inactive in this period.

The “embedded liberalism” framework promise at the Bretton Woods was to assure the policy national autonomy while pursuing external obligation of liberalisation of trade and payments. However, in the UK, at first multilateralism was regarded as very difficult to achieve from early period. On the domestic side, reconstruction from the war was gradually proceeded with monetary policy sacrificed, but the problem of inflationary economy and lack of competitiveness in the industry remained. The IMF rules which had expected to mediate external liberalisation and domestic policy management was not effectuated often.

The balance of payments crisis in 1951 gave the room for the policy-makers who attached more importance to the stability of money, and wanted to revive market mechanism to propose new policy, criticising existing policy management and fixed rate regime under the IMF. “Operation

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95 NA: T230/263, UK record of conversations with Belgian expert, 15th and 16th May.

96 The Belgians had already proposed to raise the ration of gold payments by debtors from 40% to 50% to the Managing Board of the EPU.

97 NARRA: RG469, NND887841, Belgian Position on British Plans for convertibility, February 27, 1953.

98 NA: T230/263, UK record of a discussion with M. Marjolin and Cohen, 12th June, 1953.

Robot" and "Collective Approach" were both intended to restructure international economic system and internal economy, relying much on the market mechanism.

On the side of the continental Europe too, there were feelings of disappointment to the Bretton Woods and Marjolin even thought of the application of the EPU to the Atlantic framework. However, Even though the Bretton Woods was not reliable, they never supported "Collective Approach" by the UK. it was not British plan but the OEEC and the EPU framework which could be practicable to European liberalisation of trade and finance.

Thus, although the UK and the Continentals were never reached the same opinion on "Collective Approach" and the role of the EPU, in the early 1950's both in the UK and in the continental Europe, there has already been a movement to get rid of "embedded liberalism" framework basing Keynesianism and Bretton Woods.

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