

## PART 5

# THE NEW DEAL AND THE INTERNATIONAL MONETARY SYSTEM



## **The New Deal and the International Monetary System\***

**T**he international monetary policies of the New Deal may be divided into two decisive and determining actions, one at the beginning of the New Deal and the other at its end. The first was the decision, in early 1933, to opt for domestic inflation and monetary nationalism, a course that helped steer the entire world onto a similar path during the remainder of the decade. The second was the thrust, during World War II, to reconstitute an international monetary order, this time built on the dollar as the world's "key" and crucial currency. If we wished to use lurid terminology, we might call these a decision for dollar nationalism and dollar imperialism respectively.

### **THE BACKGROUND OF THE 1920S**

It is impossible to understand the first New Deal decision for dollar nationalism without setting that choice in the monetary world of the 1920s, from which the New Deal emerged. Similarly, it is impossible to understand the monetary system of the 1920s without reference to the pre-World War I monetary order and its breakup during the war; for the world of the 1920s was an attempt to reconstitute an international monetary order,

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seemingly one quite similar to the status quo ante, but actually based on very different principles and institutions.

The prewar monetary order was genuinely “international”; that is, world money rested not on paper tickets issued by one or more governments but on a genuine economic commodity—gold—whose supply rested on market supply-and-demand principles. In short, the international gold standard was the monetary equivalent and corollary of international free trade in commodities. It was a method of separating money from the State just as enterprise and foreign trade had been so separated. In short, the gold standard was the monetary counterpart of *laissez-faire* in other economic areas.

The gold standard in the prewar era was never “pure,” no more than was *laissez-faire* in general. Every major country, except the United States, had central banks which tried their best to inflate and manipulate the currency. But the system was such that this intervention could only operate within narrow limits. If one country inflated its currency, the inflation in that country would cause the banks to lose gold to other nations, and consequently the banks, private and central, would before long be brought to heel. And while England was the world financial center during this period, its predominance was market rather than political, so it too had to abide by the monetary discipline of the gold standard. As H. Parker Willis described it:

Prior to the World War the distribution of the metallic money of gold standard countries had been directed and regulated by the central banks of the world in accordance with the generally known and recognized principles of international distribution of the precious metals. Free movement of these metals and freedom on the part of the individual to acquire and hold them were general. Regulation of foreign exchange . . . existed only sporadically, . . . and was so conducted as not to interfere in any important degree with the disposal of holding of specie by individuals or by banks.<sup>1</sup>

<sup>1</sup>H. Parker Willis, *The Theory and Practice of Central Banking* (New York: Harper and Bros., 1936), p. 379.

The advent of the World War disrupted and rended this economic idyll, and it was never to return. In the first place, all of the major countries financed the massive war effort through an equally massive inflation, which meant that every country except the United States, even including Great Britain, was forced to go off the gold standard, since they could no longer hope to redeem their currency obligations in gold. The international order not only was sundered by the war, but also split into numerous separate, competing, and warring currencies, whose inflation was no longer subject to the gold restraint. In addition, the various governments engaged in rigorous exchange control, fixing exchange rates and prohibiting outflows of gold; monetary warfare paralleled the broader economic and military conflict.

At the end of the war, the major powers sought to reconstitute some form of international monetary order out of the chaos and warring economic blocs of the war period. The crucial actor in this drama was Great Britain, which was faced with a series of dilemmas and difficulties. On the one hand, Britain not only aimed at reestablishing its former eminence, but it meant to use its victorious position and its domination of the League of Nations to work its will upon the other nations, many of them new and small, of post-Versailles Europe. This meant its monetary as well as its general political and economic dominance. Furthermore, it no longer felt itself bound by old-fashioned *laissez-faire* restraints from exerting frankly political control, nor did it any longer feel bound to observe the classical gold-standard restraints against inflation.

While Britain's appetite was large, its major dilemma was its weakness of resources. The wracking inflation and the withdrawal from the gold standard had left the United States, not Great Britain, as the only "hard," gold-standard country. If Great Britain were to dominate the postwar monetary picture, it would somehow have to take the United States into camp as its willing junior partner. From the classic prewar pound-dollar par of \$4.86 to the pound, the pound had fallen on the international

money markets to \$3.50, a substantial 30-percent drop, a drop that reflected the greater degree of inflation in Great Britain than in the U.S. The British then decided to constitute a new form of international monetary system, the “gold-exchange standard,” which it finally completed in 1925. In the classical, prewar gold standard, each country kept its reserves in gold, and redeemed its paper and bank currencies in gold coin upon demand. The new gold-exchange standard was a clever device to permit Britain and the other European countries to remain inflated and to continue inflating, while enlisting the United States as the ultimate support for all currencies. Specifically, Great Britain would keep its reserves, not in gold but in dollars, while the smaller countries of Europe would keep *their* reserves, not in gold but in pounds sterling. In this way, Great Britain could pyramid inflated currency and credit on top of dollars, while Britain’s client states could pyramid *their* currencies, in turn, on top of pounds. Clearly, this also meant that *only* the United States would remain on a gold-coin standard, the other countries “redeeming” only in foreign exchange. The instability of this system, with pseudo-gold-standard countries pyramiding on top of an increasingly shaky dollar-gold base, was to become evident in the Great Depression.

But the British task was not simply to induce the United States to be the willing guarantor of all the shaky and inflated currencies of war-torn Europe. For Great Britain might well have been able to return to the original form of gold standard at a new, realistic, depreciated parity of \$3.50 to the pound. But it was not willing to do so. For the British dream was to restore, even more glowingly than before, British financial preeminence, and if it depreciated the pound by 30 percent, it would thereby acknowledge that the dollar, not the pound, was the world financial center. This it was fiercely unwilling to do; for restoration of dominance, for the saving of financial face, it would return at the good old \$4.86 or bust in the attempt. And bust it almost did. For to insist on returning to gold at \$4.86, even on the new, vitiated, gold-exchange basis, was to mean that the pound would be absurdly expensive in relation to the

dollar and other currencies, and would therefore mean that, at current inflated price levels, Britain's exports—its economic lifeline—would be severely crippled, and a general depression would ensue. And indeed, Britain suffered a severe depression in her export industries—particularly coal and textiles—throughout the 1920s. If she insisted on returning at the overvalued \$4.86, there was only one hope for keeping her exports competitive in price: a massive domestic deflation to lower price and wage levels. While a severe deflation is difficult at best, Britain now found it impossible, for the new system of national unemployment insurance and the new-found strength of trade unions made wage-cutting politically unthinkable.

But if Britain would not or could not make its exports competitive by returning to gold at a depreciated par or by deflating at home, there was a third alternative which it could pursue, and which indeed marked the key to the British international economic policy of the 1920s: it could induce or force *other* countries to inflate, or themselves to return to gold at overvalued pars; in short, if it could not clean up its own economic mess, it could contrive to impose messes upon everyone else. If it did not do so, it would see inflating Britain lose gold to the United States, France, and other "hard-money" countries, as indeed happened during the 1920s; only by contriving for other countries, especially the U.S., to inflate also, could it check the loss of gold and therefore halt the collapse of the whole jerry-built international monetary structure.

In the short run, the British scheme was brilliantly conceived, and it worked for a time; but the major problem went unheeded: if the United States, the base of the pyramid and the sole link of all these countries to gold and hard money, were to inflate unduly, the *dollar too* would become shaky, it would lose gold at home and abroad, and the dollar would itself eventually collapse, dragging the entire structure down with it. And this is essentially what happened in the Great Depression.

In Europe, England was able to use its domination of the powerful Financial Committee of the League of Nations to

cajole or bludgeon country after country to (1) establish central banks that would collaborate closely with the Bank of England; (2) return to gold *not* in the classical gold-coin standard but in the new gold-exchange standard, which would permit continued inflation by all the countries; and (3) return to this new standard at overvalued pars so that European exports would be hobbled vis-à-vis the exports of Great Britain. The Financial Committee of the League of Nations was largely dominated and run by Britain's major financial figure, Montagu Norman, head of the Bank of England, working through such close Norman associates on the committee as Sir Otto Niemeyer and Sir Henry Strakosch, leaders in the concept of close central-bank collaboration to "stabilize" (in practice, to raise) price levels throughout the world. The distinguished British economist Sir Ralph Hawtrey, director of Financial Studies at the British Treasury, was one of the first to advocate this system, as well as to call for the general European adoption of a gold-exchange standard. In the spring of 1922, Norman induced the League to call the Genoa Conference, which urged similar measures.<sup>2</sup>

The British scarcely confined their pressure upon European countries to resolutions and conferences. Using the carrot of loans from England and the United States and the stick of political pressure, Britain induced country after country to order its monetary affairs to suit the British—that is, to return only to a gold-exchange standard at overvalued pars that would hamper their own exports and stimulate imports from Great Britain. Furthermore, the British also used their inflated, cheap credit to lend widely to Europe in order to stimulate their own flagging export market. A trenchant critique of British policy was recorded in the diary of Émile Moreau, governor of the Bank of France, a country that clung to the gold standard and to a hard-money policy, and was thereby instrumental in bringing down the pound and British financial domination in 1931. Moreau wrote:

<sup>2</sup>See Murray N. Rothbard, *America's Great Depression*, 3rd ed. (Kansas City, Mo.: Sheed and Ward, 1975), pp. 159 ff.

England having been the first European country to reestablish a stable and secure money [sic] has used that advantage to establish a basis for putting Europe under a veritable financial domination. The Financial Committee [of the League of Nations] at Geneva has been the instrument of that policy. The method consists of forcing every country in monetary difficulty to subject itself to the Committee at Geneva, which the British control. The remedies prescribed always involve the installation in the central bank of a foreign supervisor who is British or designated by the Bank of England, and the deposit of a part of the reserve of the central bank at the Bank of England, which serves both to support the pound and to fortify British influence. To guarantee against possible failure they are careful to secure the cooperation of the Federal Reserve Bank of New York. Moreover, they pass on to America the task of making some of the foreign loans if they seem too heavy, always retaining the political advantage of these operations.

England is thus completely or partially entrenched in Austria, Hungary, Belgium, Norway, and Italy. She is in the process of entrenching herself in Greece and Portugal. She seeks to get a foothold in Yugoslavia and fights us cunningly in Rumania. . . . The currencies will be divided into two classes. Those of the first class, the dollar and the pound sterling, based on gold and those of the second class based on the pound and the dollar—with a part of their gold reserves being held by the Bank of England and the Federal Reserve Bank of New York. The latter moneys will have lost their independence.<sup>3</sup>

<sup>3</sup>Émile Moreau diary entry of February 6, 1928. Lester V. Chandler, *Benjamin Strong, Central Banker* (Washington, D.C.: The Brookings Institution, 1958) pp. 379–80. On the gold-exchange standard and European countries being induced to overvalue their currencies, see H. Parker Willis, “The Breakdown of the Gold Exchange Standard and its Financial Imperialism,” *The Annalist* (October 16, 1931): 626 ff.; and William Adams Brown, Jr., *The International Gold Standard Reinterpreted, 1914–1934* (New York: National Bureau of Economic Research, 1940), 2, pp. 732–49.

Inducing the United States to support and bolster the pound and the gold-exchange system was vital to Britain's success, and this cooperation was ensured by the close ties that developed between Montagu Norman and Benjamin Strong, governor of the Federal Reserve Bank of New York, who had seized effective and nearly absolute control of Federal Reserve operations from his appointment at the inception of the Fed in 1914 until his death in 1928. This control over the Fed was achieved over the opposition of the Federal Reserve Board in Washington, which generally opposed or grumbled at Strong's Anglophile policies. Strong and Norman made annual trips to visit each other, all of which were kept secret not only from the public but from the Federal Reserve Board itself.

Strong and the Federal Reserve Bank of New York propped up England and the gold-exchange standard in numerous ways. One was direct lines of credit, which the New York bank extended, in 1925 and after, to Britain, Belgium, Poland, and Italy, to subsidize their going to a gold-exchange standard at overvalued pars. More directly significant was a massive monetary inflation and credit expansion which Strong generated in the United States in 1924 and again in 1927, for the purpose of propping up the pound. The idea was that gold flows from Britain to the United States would be checked and reversed by American credit expansion, which would prop up or raise prices of American goods, thereby stimulating imports from Great Britain, and also lower interest rates in the U.S. as compared to Britain. The fall in interest rates would further stimulate flows of gold from the U.S. to Britain and thereby check the results of British inflation and overvaluation of the pound. Both times, the inflationary injection worked, and prevented Britain from reaping the results of its own inflationary policies, but at the high price of inflation in the United States, a dangerous stock market and real estate boom, and an eventual depression. At the secret central-bank conference of July 1927 in New York, called at the behest of Norman, Strong agreed to this inflationary credit expansion over the objections

of Germany and France, and Strong gaily told the French representative that he was going to give “a little *coup de whiskey* to the stock market.” It was a *coup* for which America and the world would pay dearly.<sup>4</sup>

The Chicago business and financial community, not having Strong’s ties with England, protested vigorously against the 1927 expansion, and the Federal Reserve Bank of Chicago held out as long as it could against the expansion of cheap money and the lowering of interest rates. The *Chicago Tribune* went so far as to call for Strong’s resignation, and perceptively charged that discount rates were being lowered in the interests of Great Britain. Strong, however, sold the policy to the middle West with the rationale that its purpose was to help the American farmer by means of cheap credit. In contrast, the English financial community hailed the work of Norman in securing Strong’s support, and *The Banker* of London lauded Strong as “one of the best friends England ever had.” *The Banker* praised the “energy and skillfulness he [Strong] has given to the service of England” and exulted that “his name should be associated with that of Mr. [Walter Hines] Page as a friend of England in her greatest need.”<sup>5</sup>

<sup>4</sup>On the *coup de whiskey*, see Charles Rist, “Notice Biographique,” *Revue d’Economie Politique* (November–December, 1955): 1005; translation mine. On the Strong-Norman collaboration, see also Lawrence E. Clark, *Central Banking Under the Federal Reserve System* (New York: Macmillan, 1935), pp. 307–21; and Benjamin M. Anderson, *Economics and the Public Welfare: Financial and Economic History of the United States, 1914–1946* (New York: D. Van Nostrand, 1949).

<sup>5</sup>*The Banker*, June 1, 1926, and November 1928. In Clark, *Central Banking Under the Federal Reserve*, pp. 315–16. See also Anderson, pp. 182–83; Benjamin H. Beckhart, “Federal Reserve Policy and the Money Market, 1923–1931,” in *The New York Money Market* (New York: Columbia University Press, 1931) 4, pp. 67ff. In the autumn of 1926, a leading American banker admitted that bad consequences would follow Strong’s cheap-money policy, but added, “that cannot be helped. It is the price we must pay for helping Europe.” H. Parker Willis, “The Failure of the Federal Reserve,” *North American Review* (1929): 553.

A blatant example of Strong's intervention to help Norman and his policy occurred in the spring of 1926, when one of Norman's influential colleagues proposed a full gold-coin standard in India. At Norman's request, Strong and a team of American economists rushed to England to ward off the plan, testifying that a gold drain to India would check inflation in other countries, and instead successfully backed the Norman policy of a gold-exchange standard and domestic "economizing" of gold to permit domestic expansion of credit.<sup>6</sup>

The intimate Norman-Strong collaboration for joint inflation and the gold-exchange standard was not at all an accident of personality; it was firmly grounded on the close ties that both of them had with the House of Morgan and the Morgan interests. Strong himself was a product of the Morgan nexus; he had been the head of the Morgan-oriented Bankers Trust Company before becoming governor of the New York Fed, and his closest ties were with Morgan partners Henry P. Davison and Dwight Morrow, who induced him to assume his post at the Federal Reserve. J.P. Morgan and Company, in turn, was an agent of the British government and of the Bank of England, and its close financial ties with England, its loans to England and tie-ins with the American export trade, had been highly influential in inducing the United States to enter World War I on England's side.<sup>7</sup> As for Montagu Norman, his grandfather had been a partner in the London banking firm of Brown, Shipley and Company, and of the affiliated New York firm of Brown Brothers and Company, a powerful investment banking firm long associated with the House of Morgan. Norman himself had been a partner of Brown, Shipley and had

<sup>6</sup>See Rothbard, *America's Great Depression*, p. 138; and Chandler, *Benjamin Strong*, pp. 356 ff.

<sup>7</sup>Charles Callan Tansill, *America Goes to War* (Boston: Little, Brown, 1938), pp. 70–134. On the aid given by Benjamin Strong to the House of Morgan and the loans to England and France, see *ibid.*, pp. 87–88, 96–101, 106–08, 118–32.

worked for several years in the offices of Brown Brothers in the United States. Moreover, J.P. Morgan and Company played a direct collaborative role with the New York Fed, lending \$100 million of its own to Great Britain in 1925 to facilitate its return to gold, and also collaborating in futile loans to prop up the shaky European banking system during the financial crisis of 1931. It is no wonder that in his study of the Federal Reserve System during the pre-New Deal era, Dr. Clark concluded that “the New York Reserve Bank in collaboration with a private international banking house [J.P. Morgan and Company] determined the policy to be followed by the Federal Reserve System.”<sup>8</sup>

The major theoretical rationale employed by Strong and Norman was the idea of governmental collaboration to “stabilize” the price level. The *laissez-faire* policy of the classical, prewar gold standard meant that prices would be allowed to find their own level in accordance with supply and demand, and without interference by central bank manipulation. In practice, this meant a secularly falling price level, as the supply of goods rose over time in accordance with the long-run rise in productivity. And *in practice*, price stabilization really meant price *raising*: either keeping prices up when they were falling, or “reflating” prices by raising them through inflationary action by the central banks. Price stabilization therefore meant the replacement of the classical, *laissez-faire* gold standard by “managed money,” by inflationary credit expansion stimulated by the central banks.

In England, it was, as we have seen, no accident that the lead in advocating price stabilization was taken by Sir Ralph Hawtrey and various associates of Montagu Norman, including Sir Josiah Stamp, chairman of Midland Railways and a director of the Bank of England, and two other prominent directors—Sir Basil Blackett and Sir Charles Addis.

<sup>8</sup>Clark, *Central Banking Under the Federal Reserve System*, p. 343.

It long has been a myth of American historiography that bankers and big businessmen are invariably believers in “hard money” as against cheap credit or inflation. This was certainly not the experience of the New Deal or the pre-New Deal era.<sup>9</sup> While the most articulate leaders of the price stabilizationists were academic economists led by Professor Irving Fisher of Yale, Fisher was able to enlist in his Stable Money League (founded 1921), and its successor, the Stable Money Association, a host of men of wealth, bankers and businessmen, as well as labor and farm leaders. Among those serving as officers of the league and association were: Henry Agard Wallace, editor of *Wallace’s Farmer* and secretary of agriculture in the New Deal; the wealthy John G. Winant, later governor of New Hampshire; George Eastman of the Eastman-Kodak family; Frederick H. Goff, head of the Cleveland Trust Company; John E. Rovensky, executive vice president of the Bank of America; Frederic Delano, uncle of Franklin D. Roosevelt; Samuel Gompers, John P. Frey, and William Green of the American Federation of Labor; Paul M. Warburg, partner of Kuhn, Loeb and Company; Otto H. Kahn, prominent investment banker; James H. Rand, Jr., head of Remington Rand Company; and Owen D. Young of General Electric. Furthermore, the heads of the following organizations agreed to serve as ex-officio honorary vice presidents: the American Association for Labor Legislation; the American Bar Association; the American Farm Bureau Federation; the Brotherhood of Railroad Trainmen; the National Association of Credit Men; the National Association of Owners of Railroad and Public Utility Securities; the National Retail Dry Goods

<sup>9</sup>For examples of businessmen and bankers in favor of cheap money and inflation in American history, and particularly on the inflationary role of Paul M. Warburg of Kuhn, Loeb and Company during the 1920s, see Murray N. Rothbard, “Money, the State, and Modern Mercantilism,” in *Central Planning and Neo-Mercantilism*, Helmut Schoeck and James W. Wiggins, eds. (Princeton, N.J.: D. Van Nostrand, 1964), pp. 146–54.

Association; the United States Building and Loan League; the American Cotton Growers Exchange; the Chicago Association of Commerce; the Merchants Association of New York; and the heads of the bankers associations of forty-three states and the District of Columbia.<sup>10</sup>

Irving Fisher was unsurprisingly exultant over the supposed achievement of Governor Strong in stabilizing the wholesale price level during the late 1920s, and he led American economists in trumpeting the “New Era” of permanent prosperity which the new policy of managed money was assuring to America and the world. Fisher was particularly critical of the minority of skeptical economists who warned of overexpansion in the stock and real estate markets due to cheap money, and even after the stock market crash Fisher continued to insist that prosperity, particularly in the stock market, was just around the corner. Fisher’s partiality toward stock market inflation was perhaps not unrelated to his own personal role as a millionaire investor in the stock market, a role in which he was financially dependent on a cheap-money policy.<sup>11</sup>

In the general enthusiasm for Strong and the New Era of monetary and stock market inflation, the minority of skeptics was led by the Chase National Bank, affiliated with the Rockefeller interests, particularly A. Barton Hepburn, economic historian and chairman of the board of the bank, and Chase National’s chief economist, Dr. Benjamin M. Anderson, Jr. Another highly influential and indefatigable critic was Dr. H. Parker Willis, editor of the *Journal of Commerce*, formerly aide to Senator Carter Glass (D-Va.) and professor of banking at Columbia University, along with Willis’s numerous students, who included Dr. Ralph W. Robey, later to become economist at

<sup>10</sup>Irving Fisher, *Stabilised Money* (London: George Allen and Unwin, 1935), pp. 104–13, 375–89, 411–12.

<sup>11</sup>Fisher was also a partner of James H. Rand, Jr., in a card-index manufacturing firm. Fisher, pp. 387–88; Irving Norton Fisher, *My Father Irving Fisher* (New York: Comet Press, 1956), pp. 220 ff.

the National Association of Manufacturers. Another critic was Dr. Rufus S. Tucker, economist at General Motors. On the Federal Reserve Board the major critic was Dr. Adolph C. Miller, a close friend of Herbert Hoover, who joined in the criticisms of the Strong policy. On the other hand, Treasury Secretary Andrew W. Mellon, of the powerful Mellon interests, enthusiastically backed the inflationist policy. This split in the nation's leading banking and business circles was to foreshadow the split over Franklin Roosevelt's monetary departures in 1933.

### THE FIRST NEW DEAL: DOLLAR NATIONALISM

The international monetary framework of the 1920s collapsed in the storm of the Great Depression; or rather, it collapsed of its own inner contradictions in a depression which it had helped to bring about. For one of the most calamitous features of the depression was the international wave of banking failures; and the banks failed from the inflation and overexpansion which were the fruits of the managed international gold-exchange standard. Once the jerrybuilt pyramiding of bank credit had collapsed, it brought down the banking system of nation after nation; as inflation led to a piling up of currency claims abroad, the cashing in of the claims led to a well-founded suspicion of the solvency of other banks, and so the failures spread and intensified. The failures in the weak currency countries led to the accumulation of strains in other weak currency nations, and, ultimately, on the bases of the shaky pyramid: Britain and the United States.

The major banking crisis began with the near bankruptcy in 1929 of the Boden-Kredit-Anstalt of Vienna, the major bank of Austria, which had never recovered from its dismemberment at Versailles. Desperate attempts by J.P. Morgan, the House of Rothschild, and, later, the New York Fed, to shore up the bank only succeeded in a temporary rescue which committed more financial resources to an unsound bank and thereby made its ultimate failure in May 1931 all the more catastrophic. Rather than permit the outright liquidation of their banking systems,

Austria, followed by Germany and other European countries, went off the gold standard during 1931.<sup>12</sup>

But the key to the international monetary situation was Great Britain, the nub and the base for the world's gold-exchange standard. British inflation and cheap money, and the standard that had made Britain the base of the world's money, put enormous pressure on the pound sterling, as foreign holders of sterling balances became increasingly panicky and called on the British to redeem their sterling in either gold or dollars. The heavy loans by British banks to Germany during the 1920s made the pressure after the German monetary collapse still more severe. But Britain *could* have saved the day by using the classical gold-standard medicine in such crises: by raising bank interest rates sharply, thereby attracting funds to Britain from other countries. In such monetary crises, furthermore, such temporary tight money and checks to inflation give foreigners confidence that the pound will be sustained, and they then continue to hold sterling without calling on the country for redemption. In earlier crises, for example, Britain had raised its bank rate as high as 10 percent early in the proceedings, and temporarily contracted the money supply to put a stringent check to inflation. But by 1931 deflation and hard money had become unthinkable in the British political climate. And so Britain stunned the financial world by keeping its bank rate very low, never raising it above 4.5 percent, and in fact continuing to inflate sterling still further to offset gold losses abroad. As the run on sterling inevitably intensified, Great Britain cynically repudiated its own gold-exchange standard—the very monetary standard that it had forced and cajoled Europe to adopt—by coolly going off the gold standard in September 1931. Its own international monetary system was sacrificed on the altar of continued domestic inflation.<sup>13</sup>

<sup>12</sup>See Anderson, *Economics and the Public Welfare*, pp. 232 ff.

<sup>13</sup>See Lionel Robbins, *The Great Depression* (New York: Macmillan, 1934), pp. 89–99. See also Anderson, *Economics and the Public Welfare*,

The European monetary system was thereby broken up into separate and even warring currency blocs, replete with fluctuating exchange rates, exchange control, and trade restrictions. The major countries followed Britain off the gold standard, with the exception of Belgium, Holland, France, Italy, Switzerland, and the United States. Currency blocs formed with the British Empire forming a sterling bloc, with parities mutually fixed in relation to the pound. It is particularly ironic that one of the earliest effects of Britain's going off gold was that the overvalued pound, now free to fluctuate, fell to its genuine economic value, at or below \$3.40 to the pound. And so Britain's grand experiment in returning to a form of gold at an overvalued par had ended in disaster, for herself as well as for the rest of the world.

In the last weeks of the Hoover administration, a desperate attempt was made by the U.S. to restore an international monetary system; this time the offer was made to Britain to return to the gold standard at the current, eminently more sensible, par, in exchange for substantial reduction of the British war debt. No longer would Britain be forced by overvaluation to be in a chronic state of depression of its export industries. But Britain now had the nationalist bit in its teeth; and it insisted on outright "reflation" of prices back up to the pre-depression, 1929 levels. It had become increasingly clear that the powerful "price stabilizationists" were interested not so much in stabilization as in high prices, and now they would only be satisfied with an inflationary return to boom prices. Britain's rejection of the American offer proved to be fatal for any hopes of international monetary stability.<sup>14</sup>

The world's monetary fate finally rested with the United States, the major gold-standard country still remaining. Federal Reserve attempts to inflate the money supply and to

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pp. 244ff.; and Frederic Benham, *British Monetary Policy* (London: P.S. King and Son, 1932), pp. 1-45.

<sup>14</sup>Robbins, *The Great Depression*, pp. 100-21.

lower interest rates during the depression further weakened confidence in the dollar, and gold outflows combined with runs and failures of the banks to put increasing pressure on the American banking system. Finally, during the interregnum between the Hoover and Roosevelt administrations, the nation's banks began to collapse in earnest. The general bank collapse meant that the banking system, always unsound and incapable of paying more than a fraction of its liabilities on demand, could only go in either of two opposite directions. A truly laissez-faire policy would have allowed the failing banks to collapse, and thereby to engage in a swift, sharp surgical operation that would have transformed the nation's monetary system from an unsound, inflationary one to a truly "hard" and stable currency. The other pole was for the government to declare massive "bank holidays," that is, to relieve the banks of the obligation to pay their debts, and then move on to the repudiation of the gold standard and its replacement by inflated fiat paper issued by the government. It is important to realize that neither the Hoover nor the Roosevelt administrations had any intention of taking the first route. While there was a considerable split on whether or not to stay on the gold standard, no one endorsed the rigorous laissez-faire route.<sup>15</sup>

The new Roosevelt administration was now faced with the choice of retaining or going off the gold standard. While almost everyone supported the temporary "bank holidays," there was a severe split on the longer-run question of the monetary standard.

While the bulk of the nation's academic economists stood staunchly behind the gold standard, the indefatigable Irving Fisher redoubled his agitation for inflation, spurred onward by his personal desire to reinflate stock prices. Since the Stable

<sup>15</sup>See Rothbard, *America's Great Depression*, pp. 284-99; H. Parker Willis, "A Crisis in American Banking," in *The Banking Situation*, H.P. Willis and J.M. Chapman, eds. (New York: Columbia University Press, 1934), pp. 3-120.

Money Association had been supposedly dedicated to price stabilization, and what Fisher and the inflationists wanted was a drastic raising of prices, the association liquidated its assets into the new and frankly inflationist Committee for the Nation to Rebuild Prices and Purchasing Power. The Committee for the Nation, founded in January 1933, stood squarely for the “reflation” of prices back to their pre-1929 levels; stabilization of the price level was to proceed only *after* that point had been achieved. The Committee for the Nation, which was to prove crucially influential on Roosevelt’s decision, was composed largely of prominent businessmen. The committee was originated by Vincent Bendix, president of Bendix Aviation, and General Robert E. Wood, head of Sears, Roebuck and Company. They were soon joined, in the fall of 1932, by Frank A. Vanderlip, long close to Fisher and former president of the National City Bank of New York, by James H. Hand, Jr., of Remington Rand, and by Magnus W. Alexander, head of the National Industrial Conference Board.

Other members of the Committee for the Nation included: Fred H. Sexauer, president of the Dairymen’s League Cooperative Association; Frederic H. Frazier, chairman of the board of the General Baking Company; automobile magnate E.L. Cord; Lessing J. Rosenwald, chairman of Sears, Roebuck; Samuel S. Fels of Fels and Company; Philip K. Wrigley, president of William Wrigley Company; John Henry Hammond, chairman of the board of Bangor and Aroostook Railroad; Edward A. O’Neal, head of the American Farm Bureau Federation; L.J. Taber, head of the National Grange; F.R. Wurlitzer, vice president of Rudolph Wurlitzer Manufacturing Company; William J. McAveeny, president of Hudson Motor Company; Frank E. Gannett of Gannett Newspapers; and Indiana banker William A. Wirt. Interestingly enough, this same group of highly conservative industrialists was later to become the Committee for Constitutional Government, the major anti-New Deal propaganda group of the late 1930s and 1940s. Yet the committee was the major proponent of the inflationist policy of the early New Deal in reflating and abandoning the gold standard.

Also associated with the Committee for the Nation was another great influence on Franklin Roosevelt's decision: agricultural economist George F. Warren of Cornell, who, along with his colleague Frank A. Pearson, was the inspiration for the reflationist Roosevelt program of continually raising the buying price of gold.

The Committee for the Nation at first included several hundred industrial and agricultural leaders, and within a year its membership reached over two thousand. Its recommendations, beginning with going off gold and embargoing gold exports, and continuing through devaluing the dollar and raising the price of gold, were fairly closely followed by the Roosevelt administration.<sup>16</sup> For his part, Irving Fisher, in response to a request for advice by President-elect Roosevelt, had strongly urged at the end of February a frankly inflationist policy of reflation, devaluation, and leaving the gold standard without delay.<sup>17</sup> By April 19, when Roosevelt had cast the die for this policy, Fisher exulted, "Now I *am* sure—as far as we ever can be sure of anything—that we are going to snap out of this depression fast. I am now one of the happiest men in the world." In the same letter to his wife, an heiress of the substantial Hazard family fortune, Fisher added,

My next big job is to raise money for ourselves. Probably we'll have to go to Sister [his wife's sister Caroline] again. . . . I have defaulted payments the last few weeks, because I did not think it was fair to ask Sister for money when there was a real chance that I could never pay it back. I mean that if F.D.R. had followed Glass we would have been pretty surely ruined. So would Allied Chemical [in which much of his wife's family fortune was invested], and the U.S. Govt. . . . Now I can go to Sister with a clean conscience.<sup>18</sup>

<sup>16</sup>Fisher, *Stabilised Money*, pp. 108–09, 118–22, 413–14; and Jordan Schwarz, ed., *1933: Roosevelt's Decision, the United States Leaves the Gold Standard* (New York: Chelsea House, 1969), pp. 44–60, 116–20.

<sup>17</sup>Schwarz, ed., *1933: Roosevelt's Decision*, pp. 27–35.

<sup>18</sup>Fisher, *My Father Irving Fisher*, pp. 273–76.

If Irving Fisher's interest was personal as well as ideological, economic interests also underlay the concern of the Committee for the Nation. The farm groups wanted farm prices driven up, including farm export prices, which necessarily increase in terms of other currencies whenever a currency is devalued. As for the rest of the committee and other inflationists, Herbert Feis notes:

By the spring of 1933 diverse organizations and groups were crying aloud for some kind of monetary inflation or devaluation, or both. Most effective, probably, was the Committee for the Nation. Among its members were prominent merchants, such as the head of Sears, Roebuck, some journalists, some Wall Street operators and some foreign exchange speculators. Their purpose was to get the United States off the gold standard and to bring about devaluation of the dollar from which they would profit either as speculators in foreign exchange or as businessmen. Another group, more conservative, who stood to gain by devaluation were those who had already exported gold or otherwise acquired liquid deposits in foreign banks. They conceived that they were merely protecting the value of their capital. . . . Then there were the exporters—especially of farm products—who had been at a disadvantage ever since Great Britain had gone off the gold standard and the value of sterling had fallen much below its previous parity with the dollar.<sup>19</sup>

Also advocating and endorsing the decision to inflate and leave the gold standard were such conservative bankers as James P. Warburg of Kuhn, Loeb and Company, one of Roosevelt's leading monetary advisers; Chicago banker and former Vice President Charles G. Dawes; Melvin A. Traylor, president of the First National Bank of Chicago; Frank Altschul of the international banking house of Lazard Frères; and Russell C. Leffingwell, partner of J.P. Morgan and Company. Leffingwell

<sup>19</sup>Herbert Feis, "1933: Characters in Crisis," in Schwarz, ed., *1933: Roosevelt's Decision*, pp. 150–51. Feis was a leading economist for the State Department.

told Roosevelt that his action “was vitally necessary and the most important of all the helpful things you have done.”<sup>20</sup> Morgan himself hailed Roosevelt’s decision to leave the gold standard:

I welcome the reported action of the President and the Secretary of the Treasury in placing an embargo on gold exports. It has become evident that the effort to maintain the exchange value of the dollar at a premium as against depreciated foreign currencies was having a deflationary effect upon already severely deflated American prices and wages and employment. It seems to me clear that the way out of the depression is to combat and overcome the deflationary forces. Therefore I regard the action now taken as being the best possible course under the circumstances.<sup>21</sup>

Other prominent advocates of going off gold were publishers J. David Stern and William Randolph Hearst, financier James H.R. Cromwell, and Dean Wallace Donham of the Harvard Business School. Conservative Republican senators such as David A. Reed of Pennsylvania and Minority Leader Charles L. McNary of Oregon also approved the decision, and Senator Arthur Vandenberg (R-Mich.) happily declared that Americans could now compete in the export trade “for the first time in many, many months.” Vandenberg concluded that “abandonment of the dollar externally may prove to be a complete answer to our problem, so far as the currency factor is concerned.”<sup>22</sup>

Amidst this chorus of approval from leading financiers and industrialists, there was still determined opposition to going off gold. Aside from the bulk of the nation’s economists, the lead in

<sup>20</sup>Arthur M. Schlesinger, Jr., *The Coming of the New Deal* (Boston: Houghton Mifflin, 1959), p. 202.

<sup>21</sup>*New York Times*, April 19, 1933; quoted in Joseph E. Reeve, *Monetary Reform Movements* (Washington, D.C.: American Council on Public Affairs, 1943), p. 275.

<sup>22</sup>Schwarz, ed., *1933 Roosevelt’s Decision*, p. xx.

opposition was again taken by two economists with close ties to the banking community who had been major opponents of the Strong-Morgan policies during the 1920s: Dr. Benjamin M. Anderson of the Rockefeller-oriented Chase National Bank, and Dr. H. Parker Willis, editor of the *Journal of Commerce* and chief adviser to Senator Carter Glass (D-Va.), who had been secretary of the Treasury under Wilson. The Chamber of Commerce of the United States also vigorously attacked the abandonment of gold as well as price-level stabilization, and the Chamber of Commerce of New York State called for prompt return to gold.<sup>23</sup> From the financial community, leading opponents of Roosevelt's decision were Winthrop W. Aldrich, a Rockefeller kinsman and head of Chase National Bank, and Roosevelt's budget director, Lewis W. Douglas, of the Arizona mining family, who was related to the J. Henry Schröder international bankers and was eventually to become head of Mutual Life Insurance Company and ambassador to England. Douglas fought valiantly but in vain within the administration against going off gold and against the remainder of the New Deal program.<sup>24</sup>

By the end of April 1933, the United States was clearly off the gold standard, and the dollar quickly began to depreciate relative to gold and the gold-standard currencies. Britain, which a few weeks earlier had loftily rejected the idea of international stabilization, now became frightened: currency blocs and a depreciating pound to aid British exports were one thing; depreciation of the dollar to spur American exports and injure British exports was quite another. The British had the presumption to

<sup>23</sup>Fisher, *Stabilised Money*, pp. 355–56.

<sup>24</sup>On Douglas, see Schwarz, ed., *1933: Roosevelt's Decision*, pp. 135–36, 143–44, 154–58; and Schlesinger, *Coming of the New Deal*, pp. 196–97, and *passim*. Douglas resigned as budget director in 1934; his critical assessment of the New Deal can be found in his Lewis W. Douglas, *The Liberal Tradition: A Free People and Free Economy* (New York: D. Van Nostrand, 1935).

scold the United States for going off gold; they now rested their final hope for a restored international monetary system on the World Economic Conference scheduled for London in June 1933.<sup>25</sup>

Preparations for the conference had been under way for a year, under the guidance of the League of Nations, in a desperate attempt to aid the world economic and financial crisis by attempting the “restoring [of] the currencies on a healthy basis.”<sup>26</sup> The Hoover administration was planning to urge the restoration of the international gold standard, but the abandonment of gold by the Roosevelt administration in March and April 1933 changed the American position radically. As the conference loomed ahead, it was clear that there were three fundamental positions: the gold bloc—the countries still on the gold standard, headed by France—which desired immediate return to a full international gold standard with fixed exchange rates between the major currencies and gold; the United States, which now placed greatest stress on domestic inflation of the price level; and the British, supported by their Dominions, who wished some form of combination of the two. What was still unclear was whether a satisfactory compromise between these divergent views could be worked out.

At the invitation of President Roosevelt, Prime Minister Ramsay MacDonald of Great Britain and leading statesmen of the other major countries journeyed to Washington for individual talks with the president. All that emerged from these conversations were vague agreements of intent; but the most interesting aspect of the talks was an American proposal, originated by William C. Bullitt and rejected by the French, to establish a coordinated worldwide inflation and devaluation of currencies.

<sup>25</sup>Robbins, *The Great Depression*, p. 123; and Schwarz ed., *1933: Roosevelt's Decision*, p. 144.

<sup>26</sup>Leo Pasvolsky, *Current Monetary Issues* (Washington, D.C.: The Brookings Institution, 1933), p. 14.

[T]here was serious discussions of a proposal, sponsored by the United States and vigorously opposed by the gold countries, that the whole world should embark upon a “cheaper money” policy, not only through a vigorous and concerted program of credit expansion and the stimulation of business enterprise by means of public works, but also through a simultaneous devaluation, by a fixed percentage, of all currencies which were still at their pre-depression parities.<sup>27</sup>

The American delegation to London was a mixed bag, but the conservative gold-standard forces could take heart from the fact that staff economic adviser was James P. Warburg, who had been working eagerly on a plan for international currency stabilization based on gold at new and realistic parities. Furthermore, conservative Professor Oliver M.W. Sprague and George L. Harrison, governor of the New York Fed, were sent to discuss proposals for temporary stabilization of the major currencies. In contrast, the president paid no attention to the petition of eighty-five congressmen, including ten senators, that he appoint as his economic advisor to the conference the radical inflationist and anti-gold priest, Father Charles E. Coughlin.<sup>28</sup>

The World Economic Conference, attended by delegates from sixty-four major nations, opened in London on June 12. The first crisis occurred over the French suggestion for a temporary “currency truce”—a de facto stabilization of exchange rates between the franc, dollar, and pound for the duration of the conference. Surely eminently reasonable, the plan was also a clever device for an entering wedge toward a hopefully permanent stabilization of exchange rates on a full gold basis. The British were amenable, provided that the pound remained fairly cheap in relation to the dollar, so that their export advantage gained since 1931 would not be lost. On June 16, Sprague and Harrison concluded an agreement with the British and

<sup>27</sup>Ibid, p. 59.

<sup>28</sup>Robert H. Ferrell, *American Diplomacy in the Great Depression* (New York: W.W. Norton, 1957), pp. 263–64.

French for temporary stabilization of the three currencies, setting the dollar-sterling rate at about \$4.00 per pound, and pledging the United States not to engage in massive inflation of the currency for the duration of the agreement.

The American representatives urged Roosevelt to accept the agreement, with Sprague warning that “a failure now would be most disastrous,” and Warburg declaring that without stabilization “it would be practically impossible to assume a leading role in attempting [to] bring about a lasting economic peace.” But Roosevelt quickly rejected the agreement on June 17, giving two reasons: that the pound must be stabilized at no cheaper than \$4.25, and that he could not accept any restraint on his freedom of action to inflate in order to raise domestic prices. Roosevelt ominously concluded that, “it is my personal view that far too much importance is being placed on existing and temporary fluctuations.” And lest the American delegation take his reasoning as a stimulus to renegotiate the agreement, Roosevelt reminded Hull on June 20: “Remember that far too much influence is attached to exchange stability by banker-influenced cabinets.” Upon receiving the presidential veto, the British and French were indignant, and George Harrison quit and returned home in disgust; but the American delegation went ahead and issued its official statement on temporary currency stabilization on June 22. It declared temporary stabilization impermissible, “because the American government feels that its efforts to raise prices are the most important contribution it can make.”<sup>29</sup>

With temporary stabilization scuttled, the conference settled down to long-range discussions, the most important being centered in the subcommission on “immediate measures of financial reconstruction” of the Monetary and Financial Commission of the conference. The British delegation began by introducing a draft resolution, (1) emphasizing the importance of “cheap and plentiful credit” in order to raise the

<sup>29</sup>Pasvolsky, *Current Monetary Issues*, p. 70. See also Schlesinger, *Coming of the New Deal*, pp. 213–16; and Ferrell, *American Diplomacy*, p. 266.

world level of commodity prices, and (2) stating that “the central banks of the principal countries should undertake to cooperate with a view to securing these conditions and should announce their intention of pursuing vigorously a policy of cheap and plentiful money by open market operations.”<sup>30</sup> The British thus laid stress on coordinated inflation, but said nothing about the sticking point: exchange-rate stabilization. The Dutch, the Czechoslovaks, the Japanese, and the Swiss criticized the British advocacy of inflation, and the Italian delegate warned that

to put one’s faith in immediate measures for augmenting the volume of money and credit might lead to a speculative boom followed by an even worse slump. . . . A hasty and unregulated flood [of credit] would lead to destructive results.

And the French delegate stressed that no genuine recovery could occur without a sense of economic and financial security:

Who would be prepared to lend, with the fear of being repaid in depreciated currency always before his eyes? Who would find the capital for financing vast programs of economic recovery and abolition of unemployment, as long as there is a possibility that economic struggles would be transported to the monetary field? . . . In a word, without stable currency there can be no lasting confidence; while the hoarding of capital continues, there can be no solution.<sup>31</sup>

The American delegation then submitted its own draft proposal, which was similar to the British, ignored currency stability, and advocated close cooperation between all governments and central banks for “the carrying out of a policy of making credit abundantly and readily available to sound enterprise,” especially by open market operations that expanded the money supply. Also government expenditures and deficits should be synchronized between the different nations.

<sup>30</sup>Pasvolsky, *Current Monetary Issues*, pp. 71–72.

<sup>31</sup>*Ibid.*, pp. 72–74.

The difference of views between the nations on inflation and prices, however, precluded any agreement in this area at the conference. On the gold question, Great Britain submitted a policy declaration and the U.S. a draft resolution which looked forward to eventual restoration of the gold standard—but again, nothing was spelled out on exchange rates, or on the crucial question of whether restoration of price inflation should come first. In both the American and British proposals, however, even the eventual gold standard would be considerably more inflationary than it had been in the 1920s: for all domestic gold circulation, whether coin or bullion, would be abolished, and gold used only as a medium for settling international balances of payment; and all gold reserves ratios to currency would be lowered.<sup>32</sup>

As could have been predicted before the conference, there were three sets of views on gold and currency stabilization. The United States, backed only by Sweden, favored cheap money in order to raise domestic prices, with currency stabilization to be deferred until a sufficient price rise had occurred. Whatever international cooperation was envisaged would stress joint inflationary action to raise price levels in some coordinated manner. The United States, moreover, went further even than Sweden in calling for reflating wholesale prices back to 1926 levels. The gold bloc attacked currency and price inflation, pointed to the early postwar experience of severe inflation and currency depreciation, and hence insisted on stabilization of exchanges and the avoidance of depreciation. In the confused middle were the British and the sterling bloc, who wanted price reflation and cheap credit, but also wanted eventual return to the gold standard and temporary stabilization of the key currencies.

As the London conference foundered on its severe disagreements, the gold-bloc countries began to panic. For on the one hand the dollar was failing in the exchange markets, thus making American goods and currency more competitive. And what

<sup>32</sup>*Ibid.*, pp. 74–76, 158–60, 163–66.

is more, the general gloom at the conference gave international speculators the idea that in the near future many of these countries would themselves be forced to go off gold. In consequence, money began to flow out of these countries during June, and Holland and Switzerland lost more than 10 percent of their gold reserves during that month alone. In consequence, the gold countries launched a final attempt to draft a compromise resolution. The proposed resolution was a surprisingly mild one. It committed the signatory countries to reestablishing the gold standard and stable exchange rates, but it deliberately emphasized that the parity and date for each country to return to gold was strictly up to each individual country. The existing gold-standard countries were pledged to remain on gold, which was not difficult since that was their fervent hope. The nongold countries were to reaffirm their ultimate objective to return to gold, to try their best to limit exchange speculation in the meanwhile, and to cooperate with other central banks in these two endeavors. The innocuousness of the proposed declaration comes from the fact that it committed the United States to very little more than its own resolution of over a week earlier to return eventually to the gold standard, coupled with a vague agreement to cooperate in limiting exchange speculation in the major currencies.

The joint declaration was agreed upon by Sprague, Warburg, James M. Cox, head of the Monetary Commission of the conference; and Raymond Moley, who had taken charge of the delegation as a freewheeling White House adviser. Moley was assistant secretary of state and had been a monetary nationalist. Moley, however, sent the declaration to Roosevelt on June 30, urging the president to accept it, especially since Roosevelt had been willing a few weeks earlier to stabilize at a \$4.25 pound while the depreciation of the dollar during June had now brought the market rate up to \$4.40. Across the Atlantic, Undersecretary of the Treasury Dean G. Acheson, influential Wall Street financier Bernard M. Baruch, and Lewis W. Douglas also strongly endorsed the London declaration.

Not hearing immediately from the president, Moley frantically wired Roosevelt the next morning that “success even continuance of the conference depends upon United States agreement.”<sup>33</sup> Roosevelt cabled his rejection on July 1, declaring that “a sufficient interval should be allowed the United States to permit . . . a demonstration of the value of price lifting efforts which we have well in hand.” Roosevelt’s rejection of the innocuous agreement was in itself startling enough; but he felt that he had to add insult to injury, to slash away at the London conference so that no danger might exist of currency stabilization or of the reconstruction of an international monetary order. Hence he sent on July 3 an arrogant and contemptuous public message to the London conference, the famous “bombshell” message, so named for its impact on the conference.

Roosevelt began by lambasting the idea of temporary currency stabilization, which he termed a “specious fallacy,” an “artificial and temporary . . . diversion.” Instead, Roosevelt declared that the emphasis must be placed on “the sound internal economic system of a nation.” In particular,

old fetishes of so-called international bankers are being replaced by efforts to plan national currencies with the objective of giving to those currencies a continuing purchasing power which . . . a generation hence will have the same purchasing and debt-paying power as the dollar value we hope to attain in the near future. That objective means more to the good of other nations than a fixed ratio for a month or two in terms of the pound or franc.

In short, the president was now totally committed to the nationalist Fisher-Committee of the Nation program for paper money, currency inflation and very steep reflation of prices, and then stabilization of the higher internal price level. The

<sup>33</sup>Schlesinger, *Coming of the New Deal*, p. 218–21; Pasvolsky, *Current Monetary Issues*, pp. 80–82.

idea of stable exchange rates and an international monetary order could fade into limbo.<sup>34</sup> The World Economic Conference limped along aimlessly for a few more weeks, but the Roosevelt bombshell message effectively killed the conference, and the hope for a restored international monetary order was dead for a fateful decade. From here on in the 1930s, monetary nationalism, currency blocs, and commercial and financial warfare would be the order of the day.

The French were bitter and the English stricken at the Roosevelt message. The chagrined James P. Warburg promptly resigned as financial adviser to the delegation, and this was to be the beginning of the exit of this highly placed economic adviser from the Roosevelt administration. A similar fate was in store for Oliver Sprague and Dean Acheson. As for Raymond Moley, who had been repudiated by the president's action, he tried to restore himself in Roosevelt's graces by a fawning and obviously insincere telegram, only to be ousted from office shortly after his return to the States. Playing an ambivalent role in the entire affair, Bernard Baruch, who was privately in favor of the old gold standard, praised Roosevelt fulsomely for his message. "Until each nation puts its house in order by the same Herculean efforts that you are performing," Baruch wrote the president, "there can be no common denominators by which we can endeavor to solve the problems. . . . There seems to be one common ground that all nations can take, and that is the one outlined by you."<sup>35</sup>

Expressions of enthusiastic support for the president's decision came, as might be expected, from Irving Fisher and George F. Warren, who urged Roosevelt to avoid any possible

<sup>34</sup>The full text of Roosevelt's message can be found in Pasvolsky, *Current Monetary Issues*, pp. 83–84, or Ferrell, *American Diplomacy*, pp. 270–72.

<sup>35</sup>Schlesinger, *Coming of the New Deal*, p. 224. For Baruch's private views, see Margaret Coit, *Mr. Baruch* (Boston: Houghton Mifflin, 1957), pp. 432–34.

agreement that might limit “our freedom to change the dollar any day.” James A. Farley has recorded in his memoirs that Roosevelt was prompted to send his angry message by coming to suspect a plot to influence Moley in favor of stabilization by Thomas W. Lamont, partner of J.P. Morgan and Company, working through Moley’s conference aide and White House adviser, Herbert Bayard Swope, who was close to the Morgans and also a longtime confidant of Baruch. This might well account for Roosevelt’s bitter reference to the “so-called international bankers.” The situation is curious, however, since Swope was firmly on the antistabilizationist side, and Roosevelt’s London message was greeted enthusiastically by Russell Leffingwell of Morgans, who apparently took little notice of its attack on international bankers. Leffingwell wrote to the president: “You were very right not to enter into any temporary or permanent arrangements to peg the dollar in relation to sterling or any other currency.”<sup>36</sup>

From the date of the torpedoing of the London Economic Conference, monetary nationalism prevailed for the remainder of the 1930s. The United States finally fixed the dollar at \$35 an ounce in January 1934, amounting to a two-thirds increase in the gold price of the dollar from its original moorings less than a year before, and to a 40-percent devaluation of the dollar. The gold nations continued on gold for two more years, but the greatly devalued dollar now began to attract a flood of gold from the gold countries, and France was finally forced off gold in the fall of 1936, with the other major gold countries—Switzerland, Belgium, and Holland—following shortly thereafter. While the dollar was technically fixed in terms of gold, there was no further gold coin or bullion redemption within the U.S. Gold was used only as a method of clearing balances of payments, with only fitful redemption to foreign countries.

<sup>36</sup>Schlesinger, *Coming of the New Deal*, p. 224; Ferrell, *American Diplomacy in the Great Depression*, pp. 273 ff.

The only significant act of international collaboration after 1934 came in the fall of 1936, at about the time France was forced to leave the gold standard. Partly to assist the French, the United States, Great Britain, and France entered into a Tripartite Agreement with France, beginning on September 25, 1936. The French agreed to throw in the exchange-rate sponge, and devalued the franc by between one-fourth and one-third. At this new par, the three governments agreed—*not* to stabilize their currencies—but to iron out day-to-day fluctuations in them, to engage in mutual stabilization of each other's currencies only within each twenty-four-hour period. This was scarcely stabilization, but it did constitute a moderating of fluctuations, as well as politico-monetary collaboration, which began with the three Western countries and soon expanded to include the other former gold nations: Belgium, Holland, and Switzerland. This collaboration continued until the outbreak of World War II.<sup>37</sup>

At least one incident marred the harmony of the Tripartite Agreement. In the fall of 1938, while the United States and Britain were hammering out a trade agreement, the British began pushing the pound below \$4.80. At the threat of this cheapening of the pound, U.S. Treasury officials warned Secretary of the Treasury Henry Morgenthau, Jr., that if “sterling drops substantially below \$4.80, our foreign and domestic business will be adversely affected.” In consequence, Morgenthau successfully insisted that the trade agreement with Britain must include a clause that the agreement would terminate if Britain should allow the pound to fall below \$4.80.<sup>38</sup>

<sup>37</sup>On the Tripartite Agreement, see Raymond F. Mikesell, *United States Economic Policy and International Relations* (New York: McGraw-Hill, 1952), pp. 55–59; W.H. Steiner and E. Shapiro, *Money and Banking* (New York: Henry Holt, 1941), pp. 85–87, 91–93; and Anderson, *Economics and the Public Welfare*, pp. 414–20.

<sup>38</sup>Lloyd C. Gardner, *Economic Aspects of New Deal Diplomacy* (Madison, Wis.: University of Wisconsin Press, 1964), p. 107.

Here we may only touch on a fascinating historical problem which has been discussed by revisionist historians of the 1930s: To what extent was the American drive for war against Germany the result of anger and conflict over the fact that, in the 1930s' world of economic and monetary nationalism, the Germans, under the guidance of Dr. Hjalmar Schacht, went their way successfully on their own, totally outside of Anglo-American control or of the confinements of what remained of the cherished American Open Door?<sup>39</sup> A brief treatment of this question will serve as a prelude to examining the aim of the war-borne "second New Deal" of reconstructing a new international monetary order, an order that in many ways resembled the lost world of the 1920s.

German economic nationalism in the 1930s was, first of all, conditioned by the horrifying experience that Germany had had with runaway inflation and currency depreciation during the early 1920s, culminating in the monetary collapse of 1923. Though caught with an overvalued par as each European country went off the gold standard, no German government could have politically succeeded in engaging once again in the dreaded act of devaluation. No longer on gold, and unable to devalue the mark, Germany was obliged to engage in strict exchange control. In this economic climate, Dr. Schacht was particularly successful in making bilateral trade agreements with individual countries, agreements which amounted to

<sup>39</sup>For revisionist emphasis on this economic basis for the American drive toward war with Germany, see *ibid.*, *op. cit.*, pp. 98–108; Lloyd C. Gardner, "The New Deal, New Frontiers, and the Cold War: A Re-examination of American Expansion, 1933–1945," in *Corporations and the Cold War*, David Horowitz, ed. (New York: Monthly Review Press, 1969), pp. 105–41; William Appleman Williams, *The Tragedy of American Diplomacy* (Cleveland, Ohio: World Publishing, 1959), pp. 127–47; Robert Freeman Smith, "American Foreign Relations, 1920–1942," in *Towards a New Past*, Barton J. Bernstein, ed. (New York: Pantheon Books, 1968), pp. 245–62; and Charles Callan Tansill, *Back Door to War* (Chicago: Henry Regnery, 1952), pp. 441–42.

direct “barter” arrangements that angered the United States and other Western countries in totally bypassing gold and other international banking or financial arrangements.

In the anti-German propaganda of the 1930s, the German barter deals were agreements in which Germany somehow invariably emerged as coercive victor and exploiter of the other country involved, even though they were mutually agreed upon and therefore presumably mutually beneficial exchanges.<sup>40</sup> Actually, there was nothing either diabolic or unilaterally exploitive about the barter deals. Part of the essence of the barter arrangements has been neglected by historians—the deliberate overvaluation of the exchange rates of *both* currencies involved in the deals. The German mark we have seen was deliberately overvalued as the alternative to the spectre of currency depreciation; the situation of the other currencies was a bit more complex. Thus, in the barter agreements between Germany and the various Balkan countries (especially Rumania, Hungary, Bulgaria, and Yugoslavia), in which the Balkans exchanged agricultural products for German-manufactured goods, the Balkan currencies were also fixed at an artificially overvalued rate vis-à-vis gold and the currencies of Britain and the other Western countries. This meant that Germany agreed to pay higher than world market rates for Balkan agricultural products while the latter paid higher rates for German-manufactured products.

For the Balkan countries, the point of all this was to force Balkan consumers of manufactured goods to subsidize their own peasants and agriculturists. The external consequence was that Germany was able to freeze out Britain and other Western countries from buying Balkan food and raw materials; and since the British could not compete in paying for Balkan

<sup>40</sup>Thus, see Douglas Miller, *You Can't Do Business With Hitler* (Boston, 1941), esp. pp. 73–77; and Michael A. Heilperin, *The Trade of Nations* (New York: Alfred Knopf, 1947), pp. 114–17. Miller was commercial attaché at the U.S. Embassy in Berlin throughout the 1930s.

produce, the Balkan countries, in the bilateral world of the 1930s, did not have sufficient pounds or dollars to buy manufactured goods from the West. Thus, Britain and the West were deprived of raw materials and markets for their manufactures by the astute policies of Hjalmar Schacht and the mutually agreeable barter agreements between Germany and the Balkan and other, including Latin American, countries.<sup>41</sup> May not Western anger at successful German competition through bilateral agreements, and Western desire to liquidate such competition, have been important factors in the Western drive for war against Germany?

Lloyd Gardner has demonstrated the early hostility of the United States toward German economic controls and barter arrangements, its attempts to pressure Germany to shift to a multilateral, "Open-Door" system for American products, and the repeated American rebuffs to German proposals for bilateral exchanges between the two countries. As early as June 26, 1933, the influential American consul-general at Berlin, George Messersmith, was warning that such continued policies would make "Germany a danger to world peace for years to come."<sup>42</sup> In pursuing this aggressive policy, President Roosevelt overrode Agricultural Adjustment Administration chief George Peek, who favored accepting bilateral deals with Germany and, perhaps not coincidentally, was to be an ardent "isolationist" in the late 1930s. Instead, Roosevelt followed the policy of the leading interventionist and spokesman for an "Open Door" to American products, Secretary of State Cordell Hull, as well as assistant secretary, Francis B. Sayre, son-in-law of Woodrow Wilson. By 1935, American officials were calling

<sup>41</sup>For an explanation of the workings of the German barter agreements, see Ludwig von Mises, *Human Action* (New Haven, Conn.: Yale University Press, 1949), pp. 796–99. Also on the agreements, see Hjalmar Schacht, *Confessions of "The Old Wizard"* (Boston: Houghton Mifflin, 1956), pp. 302–05.

<sup>42</sup>Lloyd Gardner, *New Deal Diplomacy*, p. 98.

Germany an “aggressor” because of its successful bilateral trade competition, and Japan was similarly castigated for much the same reasons. By late 1938, J. Pierrepont Moffat, head of the Western European Affairs Division of the State Department, was complaining that German control of Central and Eastern Europe would mean “a still further extension of the area under a closed economy.” And, more specifically, in May 1940, Assistant Secretary of State Breckenridge Long warned that a German-dominated Europe would mean that “every commercial order will be routed to Berlin and filled under its orders somewhere in Europe rather than in the United States.”<sup>43</sup> And shortly before American entry into the war, John J. McCloy, later to be U.S. high commissioner of occupied Germany, was to write in a draft for a speech by Secretary of War Henry Stimson:

With German control of the buyers of Europe and her practice of governmental control of all trade, it would be well within her power as well as the pattern she has thus far displayed, to shut off our trade with Europe, with South America and with the Far East.<sup>44</sup>

Not only were Hull and the United States ardent in pressing an anti-German policy against its bilateral trade system, but sometimes Secretary Hull had to whip even Britain into line. Thus, in early 1936, Cordell Hull warned the British ambassador that the “clearing arrangements reached by Britain with Argentina, Germany, Italy and other countries were handicapping the efforts of this Government to carry forward its broad program with the favored-nation policy underlying it.” The tendency of these British arrangements was to “drive straight toward bilateral trading,” and they were therefore milestones on the road to war.<sup>45</sup>

<sup>43</sup>Smith, “American Foreign Relations, 1920–1942,” p. 247; Lloyd Gardner, *New Deal Diplomacy*, p. 99.

<sup>44</sup>Lloyd Gardner, “New Deal, New Frontiers,” p. 118.

<sup>45</sup>Tansill, *Back Door to War*, p. 441.

One of the United States government's biggest economic worries was the growing competition of Germany and its bilateral trade in Latin America. As early as 1935, Cordell Hull had concluded that Germany was "straining every tendon to undermine United States trading relations with Latin America."<sup>46</sup> A great deal of political pressure was used to combat German competition. Thus, in the mid-1930s, the American Chamber of Commerce in Brazil repeatedly pressed the State Department to scuttle the Germany-Brazil barter deal, which the chamber termed the "greatest single obstacle to free trade in South America." Brazil was finally induced to cancel its agreement with Germany in exchange for a \$60 million loan from the U.S. America's exporters, grouped in the National Foreign Trade Council, issued resolutions against German trade methods, and pressured the government for stronger action. And in late 1938 President Roosevelt asked Professor James Harvey Rogers, an economist and disciple of Irving Fisher, to make a currency study of all of South America in order to minimize "German and Italian influence on this side of the Atlantic."

It is no wonder that German diplomats in Brazil, Chile, and Uruguay reported home that the United States was "exerting very strong pressure against Germany commercially," which included economic, commercial, and political opposition designed to drive Germany out of the Brazilian and other South American markets.<sup>47</sup>

In the spring of 1935, the German ambassador to Washington, desperately anxious to bring an end to American political and economic warfare, asked the United States what Germany could do to end American hostilities. The American answer, which amounted to a demand for unconditional economic surrender, was that Germany abandon its economic policy in

<sup>46</sup>Smith, "American Foreign Relations, 1920-1942," p. 247.

<sup>47</sup>Lloyd Gardner, *New Deal Diplomacy*, pp. 59-60.

favor of America. The American reply “really meant,” noted Pierrepont Moffat, “a fundamental acceptance by Germany of our trade philosophy, and a thoroughgoing partnership with us along the road of equality of treatment and the reduction of trade barriers.” The United States further indicated that it was interested that Germany accept, not so much the *principle* of the most-favored national clause in all international trade, but specifically for *American* exports.<sup>48</sup>

When war broke out in September 1939, Bernard Baruch’s reaction was to tell President Roosevelt that “if we keep our prices down there is no reason why we shouldn’t get the customers of the belligerent nations that they have had to drop because of the war. And in that event,” Baruch exulted, “Germany’s barter system will be destroyed.”<sup>49</sup> But particularly significant is the retrospective comment made by Secretary Hull:

[W]ar did not break out between the United States and any country with which we had been able to negotiate a trade agreement. It is also a fact that, with very few exceptions, the countries with which we signed trade agreements joined together in resisting the Axis. The political lineup follows the economic lineup.<sup>50</sup>

<sup>48</sup>*Ibid.*, p. 103. It might be noted that in the spring of 1936, Secretary Hull refused to settle for a bilateral deal to sell Germany a large store of American cotton; Hull denounced the idea as “blackmail.” The predictable result was that in the next couple of years the sources of raw cotton imported into Germany shifted sharply from the United States to Brazil and Egypt, which had been willing to make barter sales of cotton. *Ibid.*, p. 104; Arthur Schweitzer, *Big Business in the Third Reich* (Bloomington: Indiana University Press, 1964), p. 316.

<sup>49</sup>Francis Neilson, *The Tragedy of Europe* (Appleton, Wis.: C.C. Nelson, 1946), 5, p. 289. For a brief but illuminating study of German-American trade and currency hostility in the 1930s leading to World War II, see Thomas H. Etzold, *Why America Fought Germany in World War II* (St. Louis: Forums in History, Forum Press, 1973).

<sup>50</sup>Cordell Hull, *Memoirs of Cordell* (New York, 1948), 1, p. 81.

Considering that Secretary Hull was a leading maker of American foreign policy throughout the 1930s and through World War II, it is certainly a possibility that his remarks should be taken, not as a quaint testimony to Hull's *idée fixe* on reciprocal trade, but as a positive causal statement of the thrust of American foreign policy. Read in that light, Hull's remark becomes a significant admission rather than a flight of speculative fancy. Reinforcing this interpretation would be a similar reading of the testimony before the House of Representatives in 1945 of top Treasury aide Harry Dexter White, defending the Bretton Woods agreements. White declared:

I think it [a Bretton Woods system] would very definitely have made a considerable contribution to checking the war and possibly might have prevented it. A great many of the devices which Germany and Japan utilized would have been illegal in the international sphere, had these countries been participating members.<sup>51</sup>

Is White saying that the Allies deliberately made war upon the Axis because of these bilateral, exchange control and other competitive devices, which a Bretton Woods—or for that matter a 1920s—system would have precluded?

We may take as our final testimony to the possible economic causes of World War II, the assertion by the influential *Times* of London, well after the start of the war:

One of the fundamental causes of this war has been the unrelaxing efforts of Germany since 1918 to secure wide enough foreign markets to straighten her finances at the very time when all her competitors were forced by their own debts to adopt exactly the same course. Continuous friction was inevitable.<sup>52</sup>

<sup>51</sup>Richard N. Gardner, *Sterling-Dollar Diplomacy* (Oxford: Clarendon Press, 1956), p. 141.

<sup>52</sup>*The Times* (London), October 11, 1940; quoted in Neilson, *Tragedy of Europe*, 5, p. 286.

## THE SECOND NEW DEAL: THE DOLLAR TRIUMPHANT

Whether and to what extent German economic nationalism was a cause for the American drive toward war, one point is certain: that even before official American entry into the war, one of America's principal war aims was to reconstruct an international monetary order. A corollary aim was to replace economic nationalism and bilateralism by the Hullian kind of multilateral trading and "Open Door" for American goods. But the most insistent drive, and the particularly successful one, was to reconstruct an international monetary system. The system in view was to resemble the gold-exchange system of the 1920s quite closely. Once again, all the major world's currencies were to abandon fluctuating and nationally determined exchange rates on behalf of fixed parities with other currencies and of all of them with gold. Once again, there was to be no full-fledged or internal gold standard for any of these nations; while in theory all currencies were to be fixed in terms of one key currency, which would form a gold-exchange standard on which other nations could pyramid their own supply of domestic money. But there were two crucial differences from the 1920s. One was that while the key currency was to be the only currency redeemable in gold, there was to be no further embarrassing possibility of internal redemption in gold; gold was only to be a method of international payment between central banks, and never again an actual money held by the public. In this way, the key currency—and the rest of the world in response—could expand and inflate much further than in the 1920s, freed as they were from the check of domestic redemption. But the second difference was more politically far-reaching: for instead of two joint-partner key currencies, the pound and the dollar, with the dollar as workhorse junior subaltern, the only key currency now was to be the dollar, which was to be fixed at \$35 to the gold ounce. The pound had had it; and just as the United States was to use World War II to replace British imperialism with its own far-flung empire, so in the monetary sphere the United

States was now to move in and take over, with the pound no less subordinate than all the other major currencies. It was truly a triumphant “dollar imperialism” to parallel the imperial American thrust in the political sphere. As Secretary of the Treasury Henry Morgenthau, Jr., was later to express it, the critical and eminently successful objective was “to move the financial center of the world” from London to the United States Treasury.<sup>53</sup> And all this eminently was in keeping with the prophetic vision of Cordell Hull, the man who, in the words of Gabriel Kolko, had “the basic responsibility for American political and economic planning for the peace.” For Hull had urged upon Congress as far back as 1932 that America “gird itself, yield to the law of manifest destiny, and go forward as the supreme world factor economically and morally.”<sup>54</sup>

World War II was the occasion for a new coalition to form behind the New Deal, a coalition which reintegrated many conservative “internationalist” financial interests who had been thrown into opposition by the domestic statism or economic nationalism of the earlier New Deal. This reintegration of the entire conservative financial community was particularly true in the field of international economic and monetary policy. Here, Dr. Leo Pasvolsky, a conservative economist who had broken with the New Deal upon the scuttling of the London Economic Conference, returned to a crucial role as Secretary Hull’s special adviser on postwar planning. Dean Acheson, also disaffected by the radical monetary measures of 1933–34, was now back as assistant secretary of state for economic affairs. And when the ailing Cordell Hull retired in late 1944, he was replaced by Edward Stettinius, the son of a Morgan partner and himself former president of Morgan-oriented U.S. Steel. Stettinius chose as his assistant secretary for economic affairs the

<sup>53</sup>Richard Gardner, *Sterling-Dollar Diplomacy*, p. 76.

<sup>54</sup>Smith, “American Foreign Relations, 1920–1942,” p. 252; Gabriel Kolko, *The Politics of War: The World and United States Foreign Policy, 1943–1945* (New York: Random House, 1968), pp. 243–44.

man who quickly became the key official for postwar international economic planning, William L. Clayton, a former leader of the anti-New Deal Liberty League, and chairman and major partner of Anderson, Clayton and Company, the world's largest cotton export firm. Clayton's major focus in postwar planning was to promote and encourage American exports—with cotton, not unnaturally, never out of the forefront of his concerns.<sup>55</sup>

Even before American entry into the war, U.S. economic war aims were well-defined and rather brutally simple: they hinged on a determined assault upon the 1930s system of economic and monetary nationalism, so as to promote American exports, investments, and financial dealings overseas, in short, the "Open Door" for American commerce. In the sphere of commercial policy, this took the form of pressure for reduction of tariffs on American products, and elimination of quantitative import restrictions on those products. In the allied sphere of monetary policy, it meant the breakup of powerful nationalistic currency blocs, and the restoration of an international monetary order based on the dollar in which currencies would be convertible into each other at predictable and fixed parities and there would be a minimum of national exchange controls over the purchase and use of foreign currencies.

And even as the United States prepared to enter the war to save its ally, Great Britain, it was preparing to bludgeon the British at a time of great peril to abandon their sterling bloc, which they had organized effectively after the Ottawa Agreements of 1932. World War II would presumably deal effectively with the German bilateral trade and currency menace; but what about the problem of Great Britain?

John Maynard Lord Keynes long had led those British economists who had urged a policy of all-out economic and monetary

<sup>55</sup>Kolko, *The Politics of War*, pp. 264, 485 ff.; Lloyd C. Gardner, *Architects of Illusion: Men and Ideas in American Foreign Policy, 1941–1949* (Chicago: Quadrangle Books, 1970), pp. 113–38.

nationalism on behalf of inflation and full employment. He had gone so far as to hail Roosevelt's torpedoing of the London Economic Conference because the path was then cleared for economic nationalism. Keynes's visit to Washington on behalf of the British government in the summer of 1941 now spread gloom about the British determination to continue their bilateral economic policies after the war. High State Department official J. Pierrepont Moffat despaired that "the future is clouding up rapidly and that despite the war the Hitlerian commercial policy will probably be adopted by Great Britain."<sup>56</sup>

The United States responded by putting the pressure on Great Britain at the Atlantic Conference in August 1941. Undersecretary of State Sumner Welles insisted that the British agree to remove discrimination against American exports, and abolish their policies of autarchy, exchange controls, and Imperial Preference blocs.<sup>57</sup> Prime Minister Churchill tartly refused, but the United States was scarcely prepared to abandon its crucial aim of breaking down the sterling bloc. As President Roosevelt privately told his son Elliott at the Atlantic Conference:

It's something that's not generally known, but British bankers and German bankers have had world trade pretty well sewn up in their pockets for a long time. . . . Well, now, that's not so good for American trade, is it? . . . If in the past German and British economic interests have operated to exclude us from world trade, kept our merchant shipping closed down, closed us out of this or that market, and now Germany and Britain are at war, what should we do?<sup>58</sup>

The signing of Lend-Lease agreements was the ideal time for wringing concessions from the British, but Britain consented to

<sup>56</sup>Lloyd Gardner, "New Deal, New Frontiers," p. 120.

<sup>57</sup>Richard Gardner, *Sterling-Dollar Diplomacy*, pp. 42ff.; Lloyd Gardner, *New Deal Diplomacy*, pp. 275-80.

<sup>58</sup>Smith, "American Foreign Relations, 1920-1942," p. 252; Kolko, *The Politics of War*, pp. 248-49.

sign the agreement's Article VII, which merely involved a vague commitment to the elimination of discriminatory treatment in international trade, only after intense pressure by the United States. The agreement was signed at the end of February 1942, and in return the State Department pledged to the British that the U.S. would pursue a policy of economic expansion and full employment after the war. Even under these conditions, however, Britain soon maintained that the Lend-Lease Agreement committed it to virtually nothing. To Cordell Hull, however, the agreement on Article VII was decisive and constituted "a long step toward the fulfillment, after the war, of the economic principles for which I had been fighting for half a century." The United States also insisted that other nations receiving Lend-Lease sign a virtually identical commitment to multilateralism after the war. In his first major public address in nearly a year, Hull, in July 1942, could now look forward confidently that

leadership toward a new system of international relationships in trade and other economic affairs will devolve very largely upon the United States because of our great economic strength. We should assume this leadership, and the responsibility that goes with it, primarily for reasons of pure national self-interest.<sup>59</sup>

In the postwar planning for economic affairs, the State Department was in charge of commercial and trade policies, while the Treasury conducted the planning in the areas of money and finance. In charge of postwar international financial planning for the Treasury was the economist Harry Dexter White. In early 1942, White presented his first plan, which was to be one of the two major foundations of the postwar monetary system. White's proposal was of course within the framework of American postwar economic objectives. The countries of the world were to join a Stabilization Fund, totaling \$5 billion, which would lend funds at short term to deficit countries to

<sup>59</sup>Ibid., pp. 249–51.

iron out temporary balance-of-payments difficulties. But in return for this provision of greater liquidity and short-term aid to deficit countries, exchange rates of currencies were to be fixed in relation to the dollar and hence to gold, with the gold price to be set at \$35 an ounce, and exchange controls were to be abandoned by the various nations.

While the White Plan envisioned a substantial amount of inflation to provide greater currency liquidity, the British responded with a Keynes Plan that was far more inflationary. By this time, Lord Keynes had abandoned economic and monetary nationalism for Britain under severe American pressure, and his aim was to salvage as much domestic inflation and cheap money for Britain as he could possibly induce America to accept. The Keynes Plan envisioned an International Clearing Union (ICU), which, in return for agreeing to stable exchange rates between currencies and the abandonment of exchange control, provided a huge loan fund to its members of \$26 billion. The Keynes Plan, moreover, provided for a new international monetary unit, the "bancor," which could be issued by the ICU in such large amounts as to provide almost unchecked room for inflation, even in a country with a large deficit in its balance of payments. The nations would consult with each other about correcting balance-of-payments disequilibria, through altering their exchange rates. The Keynes Plan, furthermore, provided automatic access to the fund of liquidity, with none of the embarrassing requirements, as included in the White Plan, for deficit countries to cease creating deficits by inflating their currency. Whereas the White Plan authorized the Stabilization Fund to require deficit countries to cease inflating in return for fund loans, the Keynes Plan envisioned that inflation would proceed unchecked, with all the burden of necessary adjustments to be placed on the hard-money, creditor countries, who would be expected to inflate faster themselves, in order not to gain currency from the deficit nations.

The White Plan was stringently attacked by the conservative nationalists and inflationists in Britain, particularly G.R.

Boothby, Lord Beaverbrook, *The London Times*, and *The Economist*. The Keynes Plan was attacked by conservatives in the United States, as was even the White Plan for interfering with market forces, and for automatic extension of credit to deficit countries. Critical of the White Plan were the Guaranty Survey of the Guaranty Trust Company and the American Bankers Association; furthermore, *The New York Times* and *New York Herald Tribune* called for return to the classical gold standard and attacked the large measure of governmental financial planning envisioned by both the Keynes and White proposals.<sup>60</sup>

After negotiating during 1943 and into the spring of 1944, the United States and Britain hammered out a compromise of the White and Keynes plans in April 1944. The compromise was adopted by a world economic conference in July at Bretton Woods, New Hampshire; it was Bretton Woods that was to provide the monetary framework for the postwar world.<sup>61</sup>

The compromise established an International Monetary Fund (IMF) as the stabilization mechanism; its total funds were fixed at \$8.8 billion, far closer to the White Plan's prescriptions than the Keynes. Its balance of IMF international control as against domestic autonomy lay between the White and Keynes plans, leaving the whole problem highly fuzzy. On the one hand, national access to the fund was *not* to be automatic; but on the other, the fund could no longer require corrective domestic economic policies of its members. On the question of exchange rates, the Americans yielded to the British insistence on allowing room for domestic inflation even at the expense of stable exchange rates. The compromise provided that each country could be free to make a 10-percent change in its

<sup>60</sup>Richard Gardner, *Sterling-Dollar Diplomacy*, pp. 71ff., 95–99.

<sup>61</sup>We do not deal here with the other institution established at Bretton Woods—the International Bank for Reconstruction and Development—which, in contrast to the International Monetary Fund, comes under commercial and financial, rather than monetary, policy.

exchange rate, and that larger changes could be made to correct “fundamental disequilibria”; in short, that a chronically deficit country could devalue its currency rather than check its own inflation. Furthermore, the U.S. yielded again in allowing creditor countries to suffer by permitting deficit countries to impose exchange controls on “scarce currencies.” This meant in effect that the major European countries, whose currencies would be fixed at existing highly overvalued rates in relation to the dollar, would thus be permitted to enter the IMF with chronically overvalued currencies and then impose exchange controls on “scarce,” undervalued dollars. But despite these extensive concessions, there was no “bancor”; the dollar, fixed at \$35 per gold ounce, was now to be firmly established as the key currency base of a new world monetary order. Besides, for the dollar to be undervalued and other major currencies to be overvalued greatly spurs American exports, which was one of the basic aims of the entire operation. U.S. Ambassador to Britain John G. Winant recorded the perceptive hostility to the Bretton Woods Agreement by the majority of the directors of the Bank of England; for these men saw “that if the plan is adopted financial control will leave London and sterling exchange will be replaced by dollar exchange.”<sup>62</sup>

The proposed International Monetary Fund ran into a storm of conservative opposition in the United States, from the opposite pole of the hostility of the British nationalists. The American attack on the IMF was essentially launched by two major groups: conservative Eastern bankers and Midwestern isolationists. Among the bankers, the American Bankers Association (ABA) attacked the unsound and inflationary policy of allowing debtor countries to control access to international funds; and W. Randolph Burgess, president of the ABA, denounced the provision for debtor rationing of “scarce currencies” as an “abomination.” *The New York Times*

<sup>62</sup>John G. Winant to Hull, April 12, 1944. In Richard Gardner, *Sterling-Dollar Diplomacy*, p. 123. See also *ibid.*, pp. 110–21.

urged rejection of the IMF, and proposed making loans to Britain in exchange for the abolition of exchange controls and quantitative restrictions on imports. Another bankers' group came up with a "key currency" proposal as a substitute for Bretton Woods. This key currency plan was proposed by economist John H. Williams, vice president of the Federal Reserve Bank of New York, and was endorsed by Leon Fraser, president of the First National Bank of New York, and by Winthrop W. Aldrich, head of the Chase National Bank. It envisioned a bilateral pound-dollar stabilization, fueled by a large transitional American loan, or even grant, to Great Britain. Thus, the key-currency people were ready to abandon temporarily not only the classical gold standard but even an international monetary order, and to stay temporarily in a modified version of the world of the 1930s.<sup>63</sup>

The Midwestern isolationist critics of the IMF were led by Senator Robert A. Taft (R-Ohio), who charged that, while the bulk of the valuable hard money placed in the fund would be American dollars, the dollars would be subject to international control by the fund authorities, and therefore by the debtor countries. The debtor countries could then still continue exchange controls and sterling bloc practices. Here Taft failed to realize that formal and informal structures in the Bretton Woods design would ensure effective United States control of both the IMF and the International Bank.<sup>64</sup>

<sup>63</sup>An elaboration of the banker-oriented criticisms of the International Monetary Fund may be found in Anderson, *Economics and the Public Welfare*, pp. 578–89.

<sup>64</sup>Henry W. Berger, "Senator Robert A. Taft Dissents from Military Escalation," in *Cold War Critics: Alternatives to American Foreign Policy in the Truman Years*, Thomas G. Paterson, ed. (Chicago: Quadrangle Books, 1971), pp. 174–75, 198. Taft also strongly opposed the government's guaranteeing of private foreign investments, such as were involved in the International Bank program. *Ibid.* See also Kolko, *Politics of War*, pp. 256–57; Lloyd Gardner, *New Deal Diplomacy*, p. 287; and Mikesell, *United States Economic Policy*, pp. 199f.

The administration countered the critics of Bretton Woods with a massive propaganda campaign, which was able to drive the agreement through Congress by mid-July 1945. It emphasized that the U.S. government would have effective control, at least of its own representatives in the fund. It played up—in what proved to be gross exaggeration—the favorable aspects of the various ambiguous provisions: insisting that debtor access to the fund would not be automatic, that exchange controls would be removed, and that exchange rates would be stabilized. It pushed heavily the vague idea that the fund was crucial to postwar international cooperation to keep the peace. Particularly interesting was the argument of Will Clayton and others that Bretton Woods would facilitate the general commercial policy of eliminating trade discrimination and barriers against American exports. This argument was put particularly baldly by Treasury Secretary Morgenthau in a speech to Detroit industrialists. Morgenthau promised that the Bretton Woods agreement would lead to a world trade freed from exchange controls and depreciated currencies, and that this would greatly increase the exports of American automobiles. Since the fund would begin operations the following year by accepting the existing grossly overvalued currency parities that most of the nations insisted upon, this meant that Morgenthau might have known whereof he spoke. For if other currencies are overvalued and the dollar undervalued, American exports are indeed encouraged and subsidized.<sup>65</sup>

It is perhaps understandable, then, that not only the major farm, labor, and New Deal liberal organizations pushed for Bretton Woods, but also that the large majority of industrial and financial interests also approved the agreement and urged its passage in Congress. American approval in mid-1945 was followed, after lengthy soul-searching, by the approval of Great Britain at the end of the year. By the end of its existence,

<sup>65</sup>Richard Gardner, *Sterling-Dollar Diplomacy*, pp. 136–37; Mikesell, *United States Economic Policy*, pp. 134ff.

therefore, the second New Deal had established the triumphant dollar as the base of a new international monetary order.<sup>66</sup> The dollar had displaced the pound, and within a general political framework in which the American empire had replaced the British. Looking forward perceptively to the postwar world in January 1945, Lamar Fleming, Jr., president of Anderson, Clayton and Company, wrote to his longtime colleague Will Clayton that the “British empire and British international influence is a myth already.” The United States would soon become the British protector against the emerging Russian land mass, prophesied Fleming, and this would mean “the absorption into [the] American empire of the parts of the British Empire which we will be willing to accept.”<sup>67</sup> As the New Deal came to a close, the triumphant United States stood ready to reap its fruits on a worldwide scale.

## EPILOGUE

The Bretton Woods agreement established the framework for the international monetary system down to the early 1970s. A new and more restricted international dollar-gold exchange standard had replaced the collapsed dollar-pound-gold exchange standard of the 1920s. During the early postwar years, the system worked quite successfully within its own terms, and the American banking community completely abandoned its opposition.<sup>68</sup> With European currencies inflated and overvalued, and European economies exhausted, the undervalued dol-

<sup>66</sup>On the American debate over Bretton Woods, see R. Gardner, *Sterling-Dollar Diplomacy*, pp. 129–43; on Bretton Woods, see also Mikesell, *United States Economic Policy*, pp. 129–35, 138 ff., 142 ff., 149–52, 155–58, 163–70.

<sup>67</sup>Kolko, *Politics of War*, p. 294.

<sup>68</sup>The removal of such classical pro-gold-standard economists as Henry Hazlitt from his post as editorial writer for *The New York Times* and Dr. B.M. Anderson from the Chase National Bank, coincided with the accommodation of the financial community to the new system.

lar was the strongest and “hardest” of world currencies, a world “dollar shortage” prevailed, and the dollar could base itself upon the vast stock of gold in the United States, much of which had fled from war and devastation abroad. But in the early 1950s, the world economic balance began slowly but emphatically to change. For while the United States, influenced by Keynesian economics, proceeded blithely to inflate the dollar, seemingly relieved of the limits imposed by the classical gold standard, several European countries began to move in the opposite direction. Under the revived influence of conservative, free-market, and hard-money-oriented economists in such countries as West Germany, France, Italy, and Switzerland, these newly recovered countries began to achieve prosperity with far less inflated currencies. Hence these currencies became ever stronger and “harder” while the dollar became softer and increasingly inflated.<sup>69</sup>

The continuing inflation of the dollar began to have two important consequences: (1) the dollar was increasingly overvalued in relation to gold; and (2) the dollar was also increasingly overvalued in relation to the West German mark, the French and Swiss francs, the Japanese yen, and other hard-money currencies. The result was a chronic and continuing deficit in the American balance of payments, beginning in the early 1950s and persisting ever since. The consequence of the chronic deficit was a continuing outflow of gold abroad and a heavy piling up of dollar claims in the central banks of the hard-money countries. Since 1960 the foreign short-term claims to American gold have therefore become increasingly greater than the U.S. gold supply. In short, just as inflation in England and the United States during the 1920s led finally to the breakdown of the international monetary order, so has inflation in

<sup>69</sup>We might mention the influence of such economists as Ludwig Erhard, Alfred Müller-Armack, and Wilhelm Röpke in Germany; President Luigi Einaudi in Italy; and Jacques Rueff in France, who had played a similar hard-money role in the 1920s and early 1930s.

the postwar key country, the United States, led to increasing strains and fissures in the triumphant dollar-order of the post-World War II world. It has become increasingly evident that an evermore inflated and overvalued dollar cannot continue as the permanently secure base of the world monetary system, and therefore that this ever more strained and insecure system cannot long continue in anything like its present form.

In fact, the postwar system has already been changed considerably, in an ultimately futile attempt to preserve its basic features. In the spring of 1968, a severe monetary run on the dollar by Europeans redeeming dollar claims led to two major changes. One was the partial abandonment of the fixed \$35-per-ounce gold price. Instead, a two-price, or "two-tier," gold price system was established. The dollar and gold were allowed to find their own level in the free gold markets of the world, with the United States no longer standing ready to support the dollar in the gold market at \$35 an ounce. On the other hand, \$35 still continued as the supposedly eternally fixed price for the world central banks, who were pledged not to sell gold in the world market. Keynesian economists were convinced that with the dollar and gold severed on the world market, the price of gold would then fall in the freely fluctuating market. The reverse, however, has occurred since the world market continued to have more faith in the soundness and the relative hardness of gold than in the increasingly inflated dollar.

The second change was the creation in 1969 of Special Drawing Rights (SDRs), a new form of "paper gold," of newly created paper which can supplement gold as an international currency reserve behind each currency. While this indeed put more backing behind the dollar, the quantity of SDRs has been too limited to make an appreciable difference to a world economy that trusts the dollar less with each passing year.

These two minor repairs, however, failed to change the fundamental overvaluation of the ever more inflated dollar. In the spring of 1971, a new monetary crisis finally led to a massive revaluation of the hard currencies. If the United States stubbornly

refused to lose face by raising the price of gold or by otherwise devaluing the dollar down to its genuine value in the world market, then the harder currencies, such as West Germany, Switzerland, and the Netherlands, found themselves reluctantly forced to raise the value of their currencies. Their alternatives—a massive calling upon the United States to redeem in gold and thereby the smashing of the façade of dollar redemption in gold—was too much of a political break with the U.S. for these nations to contemplate. For the United States, to preserve the façade of gold redemption at \$35, had been using intense political pressure on its creditors to retain their dollar balances and *not* to redeem them in gold. By the late 1960s, General Charles de Gaulle, under the influence of classical gold-standard advocate Jacques Rueff, was apparently preparing to make just such a challenge—to break the dollar standard as a move toward restoring the classical gold standard in France and much of the rest of Europe. But the French domestic troubles in the spring of 1968 ended that dream at least temporarily, as France was forced to inflate the franc for a time in order to pay the overall wage increase it had agreed upon under the threat of the general strike.

Despite these hasty repairs, it is becoming increasingly evident that they are makeshift stopgaps, and that a series of more aggravated crises will shake the international monetary order until a fundamental change is made. A hard-money policy in the United States that put an end to inflation and increased the soundness of the dollar might sustain the current system, but this is so politically remote as to hardly be a likely prognosis.

There are several possible monetary systems that might replace the present deteriorating order. The new system desired by the Keynesian economists and by the American government would be a massive extension of “paper gold” to demonetize gold completely and replace it with a new monetary unit (such as the Keynesian “bancor”) and a paper currency issued by a new world Reserve Bank. If this were achieved, then the new American-dominated world Reserve Bank would be able to

inflate any currencies indefinitely, and allow inflating currencies to pay for any and all deficits ad infinitum. While such a scheme, embodied in the Triffin Plan, the Bernstein Plan, and others, is now the American dream, it has met determined opposition by the hard-money countries, and it remains doubtful that the United States will be able to force these countries to go along with the plan.

The other logical alternative is the Rueff Plan, of returning to the classical gold standard after a massive increase in the world price of gold. But this too is unlikely, especially over powerful American opposition. Barring acceptance of a new world currency, the Americans would be content to keep inflating and simply force the hard-money countries to keep appreciating their exchange rates, but again it is doubtful that German, French, Swiss, and other exporters will be content to keep crippling themselves in order to subsidize dollar inflation. Perhaps the most likely prognosis is the formation of a new hard-money European currency bloc, which might eventually be strong enough to challenge the dollar, politically as well as economically. In that case, the dollar standard will probably fall apart, and we may see a return to the currency blocs of the 1930s, with the European bloc this time on a harder and quasi-gold basis. It is at least possible that the future will see gold and the hard European currencies at last dethrone the triumphant but increasingly uneasy dollar.