

The Keynes Plan for an International Clearing Union Reconsidered*

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I Introduction

Keynes was an international political economist as both an academic scholar and a political statesman, from his first book, *Indian Currency and Finance* (1914), to his posthumous article, "The Balance of Payments in the United States" (1946). Recently, some reexaminations of the aspect of Keynes's international political economist has been carried out.¹⁾

If we try to pay attention to this aspect of Keynes, we should bear Schumpeter's following passages in mind: "It cannot be emphasized too strongly that Keynes's advice was in the first instance always English advice, born of English problems even where addressed to other nations. Barring some of his artistic tastes, he was surpassingly insular, in philosophy, but nowhere so much as in economics. And, he was fervently patriotic ... [P]ractical Keynesianism is a seedling which cannot be transplanted into foreign soil: it dies there and become poisonous before it

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1) See, for example, Williamson (1983), (1985), Moggridge (1986), Shanderverker (1987) and Meltzer (1988).

dies. But ... left in English soil, this seedling is a healthy thing and promises both fruit and shade".²⁾ Hinted in this extract, we cannot ignore his inclination toward the patriotic and nationalistic attitude reflected by British interests when we study his works as an international political economist.

In this paper, Keynes's contribution on the formation of postwar international economic order, especially the Keynes plan for an International Clearing Union (ICU) as compared with the White plan for an International Stabilization Fund (ISF), is reconsidered within the context concerning Schumpeter's framework. As R.F. Mikesell, who worked under H.D. White as an economist in the Division of Monetary Research in the U.S. Treasury Department, reviews in retrospect, "[i]t is doubtful that Keynes' plan would have played such an important role in the debates in the absence of his considerable international prestige".³⁾ The purpose of this paper is to put Keynes's text in the historical context and to review it not as *the general theory* but as *a special theory*.

This paper will proceed as follows. Section II argues that one of the origins of the idea about the ICU was derived from the Germany currency plan by Dr. Schacht and Dr. Funk, and then considers the meaning of multilateral clearing in the Keynes plan. Next, we are concerned with two Anglo-American controversies in Section III: the first one on the proposal for the "monetisation of Unitas" after the publication of both the Keynes and White plans: the second one on the interpretation of "convertibility" in the provision of Agreement of the International Monetary Fund (IMF) after the Bretton Woods Conference. Section IV examines where the Keynes plan, especially its intention of realizing symmetry in the adjustment of balance of payments, should be placed in the theory of the "rule versus discretion" in monetary policy. Some concluding remarks are stated in Section V.

II Meaning of Multilateral Payments in the Keynes Plan

(i) Origins of the Keynes Plan

The Keynes plan for an ICU was first drafted on 8 September 1941, revised several times for a year and a half, and finally presented to Parliament as a White Paper by the British chancellor of the Exchequer on 7 April 1943. In the provision of its final version called the "Proposals for an International Clearing Union", we happen to encounter the following passages:

The particular proposal set forth below lay *no claim to originality*. They are an attempt to reduce to practical shape certain general ideas belonging to the contemporary climate of economic opinion, which have been given publicity in recent months *by writers of several different nationalities*.⁴⁾

Can we infer about who were included in "writers of several different

2) Schumpeter (1946, pp. 505-6).

3) Mikesell (1994, p. 12).

4) Horsefield (1969, Vol. 3, p. 21), italics mine.

nationalities”)? These passages first appeared in the fifth draft of the ICU (CW, 25, p. 170), dated on 3 August 1942, revised through August, and first sent to the Americans on 28 August. Considering that Keynes investigated the draft of the White plan in detail and estimated it highly in some respects just before he prepared the fifth draft (*ibid.*, pp. 158-68), it would be no doubt that one of “writers of several different nationalities” was H.D. White.⁵⁾

Another inference about such writers is E.F. Schumacher. Although the Schumacher plan was published in May 1943 immediately after the Keynes plan were published in April, it has been in private circulation since November 1942.⁶⁾ Although Moggridge insists that “there is no record of Keynes’s comments on the [Schumacher] proposal and no indication that it influenced the development of Keynes’s ideas” (*ibid.*, p. 21), the daughter of Schumacher, Barbara Wood, recorded in her father’s biography that Keynes gave his impression of Schumacher proposal to Sir Wilfred Eady. Indeed it may be recognized that Schumacher plan bears some resemblance to the Keynes plan at any rate, but it remains an unsettled question how his plan influenced the development of the Keynes plan.⁷⁾

More importantly, many sources and studies show that the ideas of the IUC were derived from the German originators, Dr. Schacht and Dr. Funk.⁸⁾ After the spring and early summer of 1932 the German monetary authorities negotiated a series of bilateral exchange clearing agreements with Germany’s trading partners.⁹⁾

5) Keynes, of course, the draft of the White plan criticized in another respects. We will point out his critics about the White plan in the next section.

6) Schumacher (1943, p. 150).

7) The Schumacher plan, called “Pooling Clearing”, was summarized as follows: (i) every country sets up an independent agency called the National Clearing Fund (NCF), which receive its own national currency from the home importers and disburses its own national currency to the home exporters; (ii) the NCF of deficit countries would be left with a balance of cash in hand and should use such cash by purchasing Treasury bills on the one hand, and the NCF of surplus countries would be in need of cash and should raise such cash by selling Treasury bills on the other hand; (iii) every country agrees to set up an clearing house called International Clearing Office (ICO) as Trustee in the pooling of uncleared balances; (iv) all cash balances accumulating in the NCF of the deficit countries are deemed to be taken over by the ICO on the other hand.

In this way, every national currency is made into a world currency, whereby the creation of a new international currency becomes unnecessary. It is important that the holding of surpluses, not being convertible into gold or interest-earning investment, becomes unprofitable and risky because the Pool’s assets always the weakest currency in the world. If the surpluses are made unattractive and potential surplus countries are discourage from achieving a surplus, they are obliged to speed up imports by an expansionist internal policy. In this sense, such plan is said to attempt to throw the the burden of adjustment primarily on the shoulder of the surplus countries (Schumacher, 1943, pp. 157-8). This Schumacher plan is a kind of the game of the old maid in which the surplus, denominated by the weakest currency, would be a joker every surplus countries wanted to part with.

8) See, for example, van Dormael (1976, ch. 1), Lück (1985) and Flanders (1989, pp.198-201). The Schacht plan which Lück made public in his paper has no relation to the Keynes plan for an ICU directly, because it is a proposal that Schacht submitted to the Young Committee in 1929-30 to resolve the German reparation paymetns and reinforce the future Bank for International Settlement (BIS).

9) Child (1958, p. 38).

The “New Plan”, which Dr. Hjalmar Schacht, the German Economic Minister and President of the Reichsbank, announced on 24 September 1934, was not a new system but a compilation of German exchange controls.¹⁰⁾ However, there remained a problem of multilaterally clearing of bilaterally unsettled balances. The “New Order”, which Dr. Walter Funk, the German Economic Minister and President of the Reichsbank, announced on 25 July 1940, was a resolution to the above problem by establishing a multilateral clearing system with Berlin as the central clearing-house for European payments. The reichsmark would be the international currency within the German-controlled area but the national currencies of the different countries would remain. Their national currencies will be stabilized in relation to reichsmark which would remain stable in relation to gold or the U.S. dollar.¹¹⁾ Mark balances in the German-Danish clearing account, for example, could also be used to settle Swedish claims. Dr. Funk insisted that this currency scheme would be entirely divorced from gold and adopted from the doctrine of nominalism by Knapp who said that “the currency does not depend for its value upon its gold cover, but on the value which the State gives it”.¹²⁾ Currency scheme under “New Order” was the first practical plan for a postwar monetary and economic order.¹³⁾

In November 1940 Keynes was asked by Harold Nicolson, the Minister of Information, to prepare a counterproposal for German propaganda of “New Order”. Keynes replied to this request:

In my opinion about three-quarters of passages quoted from the German broadcasts would be quite excellent if the name of Great Britain were substituted for German or the Axis, as the case may be. *If Funk’s plan is taken at its face value, it is excellent and just what we ourselves ought to be thinking of doing* (*ibid.*, p. 2, italics mine).

In a memorandum entitled the “Proposal to Counter the German ‘New Order’” dated on 25 December 1940, circulated on 1 December, Keynes expressed a certain sympathy with the German proposal based on Schachtian bilateralism. In the memorandum he says: “After the last war *laissez-faire* in foreign exchange led to chaos. Tariffs offers no escape from this. *But in Germany Schacht and Funk were by force of necessity to evolve something better. In practice they have used their new system to the detriment of their neighbours. But the underlying idea is sound and good*” (*ibid.*, pp. 8-9, italics mine). He goes on to say: “The most definite of the German plans, so far, is currency scheme of Dr. Funk ... It has only one merit, namely that it avoids some of abuse of the old *laissez-faire* international currency arrangement, whereby a country could be bankrupted, not because it lacked exportable goods, but merely because it lacked gold ... The arrangement we are now slowly perfecting, by which international exchange returns to what it always should have been, namely a means for trading goods against goods, will outlast the war” (*ibid.*, p. 12). Similar point was repeated

10) *ibid.*, p. 133.

11) Einzicg (1941, p. 2).

12) Guillebaud (1940, p. 456).

13) van Dormael (1978, p. 5).

in his first draft of the ICU, about ten months later:

... Dr. Schacht stumbled in desperation on something new which had in it the germs of a good technical idea. This idea was to cut the knot by discarding the use of a currency having international validity and substitute for it amounted to barter, not indeed between individuals, but between different economic units ... *[T]he fact that this method was used in service of evil must not blind us to its possible technical advantage in service of a good cause ...* I expound in a separate paper a possible means of still retaining a currency having an unrestricted international validity. *But the alternative to this is surely not a return to the currency disorders the epoch between the wars, mitigated and temporarily postponed by some liberal Red Cross work by the United States, but a refinement and improvement of Shachtian device (ibid., pp. 23-4, italics mine).*

As these quotations show, it is not surprising that Keynes regarded the techniques of German exchange control created by Schacht and Funk as a prototype of postwar international monetary system, even though the purpose of this currency scheme for enlarging German-controlled counties was to be politically blamed. The early drafts of the Clearing Union seem to be influenced by such a Germany currency scheme in some respects.

(ii) Multilateral Clearing with Exchange Controls

The ICU is based upon the “banking principle” whose assets are its reserves and loans to the central banks of member countries and whose liabilities the deposits of central banks. The deposits, called “Bancor”, is a new international currency created by the ICU. Each country is given a quota and allowed overdrafts according to this quota. The multilateral clearing is attained by the transfer of Bancor, in which the surplus countries have a credit balance with the IUC and deficit countries have a debit balance. In other words, the imbalance of the balance-of-payments is reflected in the accounts of the ICU as overdrafts for the debtors and positive balances for the creditors. Such multilateral clearing system has been thought that the Keynes plan for an ICU made a favorable comparison with the White plan for an ISF. As the ISF has no multilateral clearing system and “Unitas”, a new international currency created by the ISF, is only an unit account.

However, we should not overlook that the multilateral clearing of the ICU is not through the competitive exchange market but between central banks monopolizing all exchange transactions. In his first draft of the Clearing Union, Keynes stipulated this as follows:

Within any member-country or currency unit the provision of foreign exchange to be concentrated in the hand of its central bank which would deal with the public through the usual banks ... Internationally all transactions [should] be cleared between central banks, operating on their accounts with an International Clearing Bank (CW, 25, pp. 33-4).

Similarly, in his second draft, Keynes repeats this stipulation:

Within any state (or group of states), which is a member of the Union, the

provision of foreign exchange for remittance either to member or non-member states will be concentrated in the hands of its central bank which would deal with the public through the usual banks ... The balances due to or from any foreign state will be cleared between the central banks concerned, operating on their accounts with the Clearing Bank (*ibid.*, p. 61).

After pointing out that Keynes “envisaged multilateralising centralized exchange dealings *within the context of exchange controls and payments agreements*”, Moggridge continues that such a system of “all international payments being channeled through central banks with imbalances being multilateralised through an international institution ... ruled out *the post-1945 norm* in which commercial banks effect international payments through competitive exchange markets and leave central banks and exchange funds as residual buyers and sellers to the degree necessary to maintain the agreed or desired pattern of exchange rates”.¹⁴⁾ The Keynes plan for an ICU influenced by the German currency scheme was against “the post-1945 norm” based on private exchange transactions through competitive exchange markets. As indicated in the next section, Keynes continued to persist in his ideas of the anti-post-1945 norm, hoping to recover his lost position after the publication of both the Keynes and White plan and even after the Bretton Woods Conference.

III Anglo-American Controversy on Multilateral Payments

(i) Keynes vs. White Controversy on Monetisation of Unitas

After both Keynes and White plans were published, Keynes thought that many differences in both plans would converge on the White plan. Rather he feared that the Americans would go back into isolationism as they had used before and withdrew from the collaboration that tried to constitute postwar international economic order.¹⁵⁾ As Pressnell points out, the most important “Sterling-Dollar Diplomacy” between the publication of both plans in April 1943 and the Bretton Woods Conference in July 1944 was the Washington talks between September-October 1943.¹⁶⁾ The British delegation was led by Richard Law, then Parliamentary Under-Secretary of State at Foreign Office, but the head of the Law Mission was eventually Keynes as one of the Treasury members. In these Washington talks, the authors of the ICU and the ISF confronted one another directly.¹⁷⁾

The British War Cabinet left five instructions to the delegation: (i) members

14) Moggridge (1986, pp. 59-60), italics mine. See also Moggridge (1992, p. 673).

15) Immediately after the publication of both plans, Keynes wrote in a letter to Sir Frederick Phillips, represented the British Treasury in U.S., that what “we were in a sense propagating for the Harry White plan ... was no harm”. He continued: “The real risk is that there will be no plan at all and that [the U.S.] Congress will run away from their own proposal. No harm, therefore, at least so it seems to me, if the Americans work up a certain amount of patriotic fervour for their own version. Much can be done in detail hereafter to improve it. The great thing at this stage that they should get thoroughly committed to there being some plan” (CW, 25, p. 242).

16) Pressnell (1986, p. 116). See also Horsefield (1969, Vol. 1, p. 60) and Mikesell (1994, pp. 24-30).

17) Harrod (1951, p. 555).

should maintain the freedom to alter its own exchange rate: (ii) the Fund quota should be larger than what the Americans had proposed: (iii) gold subscription to the Fund should be limited to 12 1/2 per cent of each nation's quota: (iv) any attempt to deal with abnormal war balances should not be part of the scheme: (v) the Fund should be "passive" in the exchange market and not buy or sell national currencies.¹⁸⁾ In this section, we will examine only the fifth instruction, namely, the proposal for monetisation of Unitas, because it is thought to be closely related to the recovering his lost position of the Keynes plan.

As Keynes criticize the White plan for forgetting all about "the useful concept of bank money" (CW, 25, p. 159), Unitas in the ISF plays a roll only as an unit of account in comparison with Bancor in the ICU as a medium of exchange and reserve currency. Also, as Keynes ridicule it, the ISF is "a mixed bag of currencies" (*ibid.*, p. 308).

The April 1943 and early drafts of the White plan provided that the ISF might sell to member A the currency of member B only if A had an adverse balance of payments with B. This meant, however, that the ISF failed to provide for multi-lateral clearing. This problem had been resolved in July by amending the relevant clause to read "to meet an adverse balance of payments predominantly on current account with any member country", so that it was possible for A to require the currency of B to settle an adverse balance of payments with C, even though its balance of payments with B was favorable.¹⁹⁾ In the same draft, however, another disturbing provision was introduced: the currency purchased by the ISF had to be "in good standing". Keynes objected to this provision as follows:

[The Fund] would exercise its discretion whether or not to accept or to supply particular currencies. It would purchase only those currencies which it decided (on no clear criterion) to be 'in good standing', and (also on no clear criterion) the sale of which 'is required to meet an adverse balance of payments predominantly on current account with any member country' (*ibid.*, p. 318).

If the ISF, for example, would judge sterling to be not 'in good standing' at its discretion, the U.K. was obliged to lose the qualification which draws any currency from the fund in exchange for the sterling. As Presnell point out, Keynes "feared that the alternative of a 'a mixed bag of currencies' would permit discrimination against a particular currency, specifically against sterling, and hence, the sterling area, thereby reducing instead of increasing liquidity".²⁰⁾ Because the ISF as "a mixed bag of currencies" would be "a dealer in currencies" which receive the strong currencies in exchange for the weaker in order to maintain the quality of its portfolio, it would become "active" in management whatever its intention of remaining "passive".²¹⁾

18) CW, 25, p. 338. See also Moggridge (1992, pp. 723-4).

19) Horsefield (1969, Vol. 1, p. 59).

20) Presnell (1986, p. 122).

21) *ibid.*, p. 140.

The proposal for monetisation of Unitas was to make Unitas “bank money” and introduce the principle of “passivity” to the ISF.²²⁾ Keynes proposed:

The Fund must not deal in a mixed bag of currencies but only in unitas, which will not be redeemable in gold and holdings of which will be acquired by members in exchange for their subscriptions and transferred between them by entries in the Fund’s books ... This condition means that, in return for their initial subscription in terms of gold and securities, members would be credited with corresponding mounts of unitas on the books of Fund which would free to transfer to one another in exchange for needed foreign currency. Thus the Fund would become passive so far as exchange dealings are concerned, just as the C.U. would be passive (*ibid.*, pp. 317-8).

The British delegation formally submitted the proposal for monetisation of Unitas to the Americans in the Washington talks on 21 September. In the memorandum sent to H.D. White, Keynes proposed that a member should receive in return for subscription to the Fund a corresponding balance expressed in Unitas, that a member should undertake to sell its currency to another member and to buy it from another member in exchange for a transfer of Unitas at parity on the books of the Fund, and that the maximum commitment for a member to receive Unitas should be limited up to 120 per cent of its quota (*ibid.*, pp. 342-3). Monetisation of Unitas was to make the ISF the clearing house through Unitas, and so, eventually to realize the Keynes plan which make the the ICU the clearing house through Bancor, even though remaining the subscription principle.

This proposal was opposed by American delegates because the effect of this proposal would be the same as that of Keynes plan itself, namely to expand the U.S. commitment beyond its contribution. Although they agreed that the Fund should be passive, they insisted that the real effect of transactions between the Fund and the central bank would be the same whether Unitas was used or not.²³⁾ By the end of Washington talks Keynes and other British officials was persuaded that there was no fundamental difference between the formulation of the Fund with and without Unitas. In consequence of a compromise that the Americans accepted the principle of passivity and the British withdrew the proposal for monetisation of Unitas, the negotiation resulted in the omission from the Joint Statement, appeared on 22 April 1944, of the word “Unitas” as well as “in good standing”. Keynes prefaced the following explanatory notes with the Joint Statement:

Under the *Clearing Union* the memeber countries might have been said to bank with the Union with which they were to keep balances or run overdrafts. Under *the International Monetary Fund*, on the other hand, the Fund may be said to bank with the member countries, which undertake to grant to the Fund facilities to hold and to draw on their local funds ... These two arrangements represent alternative technical set-ups, capable of performing

22) Harrod (1951, pp. 562-3).

23) Horsefield (1969, Vol. 1, p. 65).

precisely the same functions ... As a consequence of this, it is no longer necessary to introduce a new international unit, whether bancor or unitas, since it is only if the member countries bank with the Fund that the use of a new common unit becomes unavoidable (*ibid.*, pp. 437-8).

(ii) Keynes vs. Robertson Controversy on Convertibility

Even after the Bretton Woods Conference of July 1944, Keynes persisted in his belief. It is in the Keynes-Robertson controversy on the interpretation of the convertibility in Article VIII of the IMF Agreement that he continued to hold the idea of the multilateral clearing between central banks after centralizing all exchange dealings in its central bank.²⁴⁾

There are two provisions of convertibility in Article VIII, General Obligations of Members: first, Article VIII Section 2 (a), Avoidance of Restrictions on Current Payments; secondly, Article VIII Section 4, Convertibility of Foreign Held Balances. VIII 2 (a) provides that members should not “impose restrictions on the making of payments and transfers for current international transactions” except for three set of circumstances: (i) if the scarce currency clause was invoked (Article VII Sec. 3 (b)), (ii) during the transition (Article XIV Sec. 2), (iii) with the approval of the Fund. VIII 4 provides that members should convert overseas balances into “the currency of the member making the request or gold”, if these balances had been “recently acquired as a result of current transactions” or whose “conversion is needed for making payments for current transactions”. That is to say, VIII 2 (a) prescribes for *market convertibility* on the one hand and VIII 4 demands *official convertibility* on the other hand.²⁵⁾

On 31 July 1944 immediately after the Bretton Woods Conference came to an end, Dennis Robertson sent a note to Keynes in Ottawa. In this note, Robertson stated that VIII 2 (a) was “the main and over-riding obligation” and that VIII 4 was “the supplementary obligation” (CW, 26, pp. 114-5). He went on to say that “[i]t follows ... that the clause exempting a member which has exhausted its rights of resources to the Fund from its obligations under VIII 4 (a) [(v)], is of very doubtful value so far as the obligation under VIII 4 (a)(i) is concerned, since ... this obligation is already implicit the master-obligation set out in VIII 2 (a), which is subject to no such let-out” (*ibid.*, p. 116). As opposed to Robertson’s interpretation about relation between VIII 2 (a) and VIII 4, Keynes denied VIII 2 (a) involved an obligation of convertibility. He stated that “[c]onvertibility only comes about, if at all, through the combination of this clause [VIII 2 (a)] with VIII 4” (*ibid.*, p. 118). Keynes’s interpretation about the relation of this two provisions of convertibility is that a non-resident owner of sterling balances can only disposed of it through his own central bank (VIII 2 (a)); and that the only obligation of the British Central Bank is

24) There are many sources and some detail studies about the controversy. See Gold (1981a, b), Pressnell (1987, pp. 170-182), and Moggridge (1992, pp. 748-53).

25) Gold (1981a).

to buy sterling from another central bank in exchange for the foreign exchange it desires (VIII 4 (a)); but that the British Central Bank is exempted from its obligation if it has exhausted its rights of resources to the Fund (VIII 4 (b)(v)).

In short, Keynes put emphasis on the *official convertibility* of VIII 4 on the one hand and Robertson adhered to *market convertibility* of VIII 2 (a) on the other hand. A belief of Keynes is that “[a] leading peculiarity ... in I.M.F. is that, apart from VIII 2, the obligations all apply *as between central banks and not as between a central bank and non-resident individual*” (*ibid.*, p. 119, italics mine), whereas the assumption of Robertson is that “*exchange are always maintained by supporting the free market*, instead of forcing member banks to operate through the machinery of the Fund” (*ibid.*, p. 122, italics mine). Keynes summarized the difference of his own ideas and Robertson’s as follows:

The obligation of convertibility under VIII 4—in my opinion the *only* obligation of convertibility we undertake—is between pairs of central banks and related only to convertibility between the currencies of the pair in question. It gives no rights to private persons, who can only obtain convertibility through the good offers of their own central bank. According to Professor Robertson, on the other hand, VIII 2 (a) imposes on our Exchange Control an over-riding obligation to provide any private person on request with any currency in the world. (*ibid.*, p. 135).

The controversy originating between Keynes and Robertson became the debate between the U.K. and the U.S. Treasury which lasted for almost one year. Keynes and almost every other British expert wanted the restoration of the convertibility of sterling to be postponed and a comprehensive exchange control to be maintained as long as possible. Robertson and the U.S. Treasury, however, considered that the practice for the U.K. monetary authority to centralize all exchange transactions and not to provide the exchange to the nonresident to transfer his proceeds into his own currency was a restriction and violation under VIII 2 (a).²⁶⁾ Keynes drafted the letter to H. Morgenthau, the U.S. Secretary of the Treasury, and sent it to Washington under the signature of J. Anderson, Chancellor of the Exchequer, dated on 1 February 1945.²⁷⁾ It took four months for Morgenthau’s reply to reach to London, in which Morgenthau stated that there was no inconsistency between these two sections.²⁸⁾ The U.K.-U.S. official correspondence ended by Anderson’s reply to Morgenthau dated 28 June, in which Anderson agreed that the question of inconsistency between these two sections would “not arise immediately” and might “in practice have little effect”.²⁹⁾

Although the Anglo-American debate on the convertibility was concluded ambiguously, the development of an international monetary system was vindicated Robertson’ views unambiguously. As a free exchange market has been restored

26) Gold (1981b, pp. 39-40).

27) CW, 26, pp. 175-7. See also Pressnell (1986, Appendix 16a).

28) CW, 26, pp. 183-4. See also Pressnell (1986, Appendix 17).

29) See Pressnell (1986, Appendix 18).

since the 1950s in many member countries including the U.K. VIII 4 has fallen into desuetude and indeed has never been invoked.³⁰⁾ *The mechanism of multilateral payments under market convertibility* at which VIII 2 (a) has been aimed was attained. On the other hand, VIII 4 as well as the Keynes's ICU aimed at *the mechanism of multilateral payments under official convertibility*. The reason why Keynes regarded VIII 4 as important is that its provision might make multilateral payments system through the Fund itself. However, afterwards the international monetary system developed in the direction which Keynes could not expected; a free exchange market was restored; the policy of members do not have to monopolized exchange transactions; even monetary authorities as well as private parties have been able to participate in the free exchange market. In that sense, it may be thought that both what VIII 4 has become a dead letter and what the Keynes plan for an ICU was defeated by the White plan for an ISF are on the same line.

IV The Postwar International Economic Order in the Keynes Plan

(i) Rule vs. Discretion in Keynes's early and later stance

The international economic order is defined by Williamson as "a set of generally accepted rules and conventions regarding the proper way for countries to conduct those of their economic policies that have significant repercussions outside their own borders". And "the lack of an order is characterized by at most weak rules and light-hearted breaches such rules as are supposed to exist, resulting in countries adopting policies with significant international repercussions entirely at their national discretion".³¹⁾ What is apparent in this definition is that the international economic order is stabilized when some rules are accepted by all countries lest any internal economic policy conducted by one country has significant external repercussions to other countries. Contrary to this case, an international economic order is destabilized when such rules are not accepted and every country conducts its economic policy at its own discretion.

By the way, we could roughly place the past controversies about monetary policy on the scheme of so-called "rule versus discretion", such as metallism versus nominalism, currency school versus banking school, gold standard versus managed currency, fixed exchange rate versus floating exchange rate, and monetarism versus Keynesianism.³²⁾

The basic stance of Keynes in his early days was that monetary policy should be used to attain internal stability and that the achievement of external stability had to be considered separately. British monetary policy during interwar period had a dilemma that while a cheap money policy was domestically required to reduce unemployment on the one hand, a dear money policy was externally needed to finance the

30) Gold (1981b, p. 40).

31) Williamson (1983, p. 87).

32) On the theory of rules and discretion in monetary policy, see Giovannini (1993).

deficits of balance of payments on the other. In the face of such a “fundamental disequilibrium”, the devaluation of pound sterling was the best policy choice as Keynes made rightly diagnosis. Against British government, which were going to make a decision to return to the gold standard at its pre-war parity of \$4.86, overvalued by at least 10 per cent, in 1925, Keynes, in *A Tract on Monetary Reform* (1923), proposed the managed currency system in order to be free from the rules of game in the gold standard and to able to be discretionary control money supply to adjust internal economic conditions. In this way, it is clear that Keynes placed superiority on discretion over the rules.

In the second draft of the ICU, dated on 18 November 1941, however, Keynes explained his view seemingly contradictory to his early stance mentioned above:

In only one important respect must an International Bank differ from the mode suitable to a national bank within a closed system, namely that *much more must be settled by rules and by general principles agreed beforehand and much less by day-to-day discretion* (CW, 25, p. 45, italics mine).

In his third draft, dated on 15 December 1941, on the other hand, Keynes added the following sentences to the above quotations:

Perhaps the most difficult question to determine is how much to decide by rules and how much by discretion. *If rule prevails*, the liabilities attaching to membership of the system become clear and definite, whilst the responsibilities of central management are reduced to a minimum. ... *If discretion prevails*, we have to decide how far the ultimate decision can be left to the individual members and how far to the central management. ... If rule prevails, the scheme can be made more water-tight theoretically. *If discretion prevails*, it may work better in practice. All this is the typical problem of any super-national authority. *In my first draft I was criticised for leaning too much to the side of rule. In this draft this bias is in the other direction ...* (*ibid.*, p. 73, italics mine)

Meltzer asserts that “[t]he proposals for the Clearing Union, in fact all of his proposals, show Keynes as a proponent of monetary rules intended to restrict discretionary policy and reduce uncertainty without eliminating short-term policy response. For Keynes, rules acted as general guides to action and restrictions that provide stability and reduce uncertainty”.³³⁾ He goes on to say: “On the choice between precommitment and unlimited discretion, Keynes was mainly on the side of precommitment of rules”.³⁴⁾ Moggridge, on the other hand, regarding the second quotation as more important, said that “[i]n the case of his Clearing Union Keynes started with an emphasis on rules but he moved in the direction of discretion from the third draft onwards”.³⁵⁾ How can we reconcile between Metzler’s view that Keynes shifted his stance from his early vision (discretion over rules) to his later vi-

33) Meltzer (1988, pp. 210-1).

34) *ibid.*, pp. 243-4.

35) Moggridge (1986, p. 68). See also Moggridge (1992, p. 677).

sion (rules over discretion) and Moggridge's view that Keynes's stance was constantly discretion-oriented.?

(ii) Meaning of the Symmetry in the Keynes Plan

Both Keynes and White, of course, had to devise a set of rules in order for the postwar international economic order. An essential rule of the Keynes plan is the "symmetry" in balance of payments adjustment. The problem of the asymmetry between the debtor and creditor countries has generally been known as one of the most important themes of Keynes's international political economy. The theme also has been long associated with the Keynes plan as opposed to the White plan.³⁶⁾

It is in the first draft of the ICU that his intention appears most clearly and vividly. He refers to the fact that "in the past five hundreds years there have been only two periods of about fifty years" (CW, 25, p. 21) when the adjustment mechanism of international payments can be said to have worked. The first period was the age of Elizabeth I, in the later half of 16th century, when the prodigious inflow of silver from new the new world brought inflation to Europe and "the strong, creditor countries, which first received silver, had to take the initiative in price adjustment" (*ibid.*, p. 30). The second period was the age of Victoria, in the later half of 19th century, when "the system of international investment pivoting on London transferred the onus of adjustment from debtor to the creditor position" (*ibid.*, p. 21). The inflow of gold to the main creditor centers were "immediately translated ... not into a change in prices and wages but into a change in the volume of foreign investment by the creditors" (*ibid.*, p. 30). He concludes that "the architects of a successful international system must be guided by these lessons. The object of the new system must be to require the chief initiative from the creditor countries" (*ibid.*, p. 30).

By the symmetry in the adjustment mechanism, Keynes means to put the responsibility and burden for adjustment on the creditor countries. In the Keynes plan for an ICU, this rule is to put expansionist pressure, namely, measures for the expansion of domestic credit and domestic demand, on the creditor countries. The rule of the symmetry are also materialized by the provision that even a creditor country should pay a charge on his credit balances in the ICU. Keynes regards this provision as "a significant indication that the system looks on excessive credit balances with as critical an eyes as on excessive debit balances" (*ibid.*, pp. 118-9, p. 173).

What about changes in exchange rates? Under the Keynes plan, a deficit country whose debit balance has exceeded a quarter of its quota on the average of at least a year shall be entitle to depreciate its currency within 5 per cent a year "without the permission of the Governing Board" (*ibid.*, pp. 174-5). If its debit balance has exceeded a half of its quota, the Governing Board may require depreciation of its currency. If its debit balance has exceeded three-quarters of its quota, the Gov-

36) Flanders (1989, p. 190).

erning Board may ask the further suitable remedies. A surplus country whose credit balance has exceeded a half of its quota on the average shall discuss with the Governing Board about appreciation of its currency. In this way Keynes supported the adjustable peg.³⁷⁾ On the contrary, under the White plan, exchange rates may change only in the case of “fundamental disequilibrium” and are required approval of the ISF, namely, a 4/5 majority of the members’ votes. In this regard, Keynes criticized that “there is a greater surrender of sovereignty under S.F. than under C.U., and the rigidity is very excessive” (*ibid.*, p. 220). Moggridge is correct as far as changes in exchange rates concerned when he says as mentioned above: “in the case of his Clearing Union Keynes started with an emphasis on rules but he moved in the direction of discretion from the third draft onwards”.³⁸⁾

The rule of symmetry at which Keynes aimed was his fear about that U.S. discretionary policies (especially sterilization policy) would be a heavy burden to the postwar British economic reconstitution. Indeed it might be fair that his proposal of adjustable peg was discretion-oriented, but it were also intended to constrain the biggest super-power in the postwar world. So we had better place his thought not on the scheme of “rule versus discretion” but on “rule versus power”. He formulated a postwar international monetary plan not under power-based system but under rule-based system. It is needless to say that his intention was based on his patriotism reflected by British economic interests.

Concluding Remarks

In this paper, we examined the historical constraints of the Keynes plan for an ICU. First, one of important origins of the Keynes plan was German currency scheme which aimed at a multilateral payments system of bilateral exchange clearing agreements. The multilateral clearing of the ICU is not through a competitive exchange market but between central banks monopolizing all exchange transactions. It was his early drafts of the IUC influenced by German originators that such characteristics was distinct.

Secondly, Keynes was optimistic even after it is clear that the realization of the ICU made impossible. Even though its mechanism through Bancor are not realized, he thought that if monetisation of Unitas could be agreed upon, the flame of this mechanism would be carried out in the ISF. Also even though this proposal could not be agreed upon, he thought once more that if the interpretation that the provision of official convertibility of Article VIII Section 4 is master-obligation against that of market convertibility of Article VIII Section 2 (a) could be agreed upon, the core of his ideas would remain in the IMF. All of these expectations failed to be realized because his plan for IUU, his proposal for monetisation of

37) For the view that Keynes switched his thought of exchange rate system from crawling peg to adjustable peg, see Williamson (1983, p. 99).

38) Moggridge (1986, p. 68).

Unitas in ISF and his interpretation on convertibility in the IMF were all against the “postwar norm” of a free exchange market.

Finally, the postwar international economic order at which Keynes aimed was a rule-based system rather than a power-based system that would permit the symmetry of the adjustment of balance of payments between the U.S. as the largest creditor country and the rest of the world. In order to constraint the U.S. power, he proposed, for example, the domestic expansion of the surplus countries, paying a charge even on their credit balances in the ICU, and the discretionary change of exchange rates. Such a rule-based system, however, was based on the U.K. national interests which were burdened with the large sterling balances. It was his patriotic inclination to British national interests that the multilateral clearing system in the Keynes’s sense, the convertibility in his interpretation, and the symmetrical system of the adjustment mechanism, almost all became impractical at Bretton Woods Conference and after.

By the way, Keynes’s another contribution to the postwar international economic order was the way to deal with the large sterling balances, namely “abnormal wartime balances” in the U.K. official term. Because British officials wanted to exclude this problem in the discussion at Bretton Woods Conference, the Keynes plan for an ICU seemed intentionally to avoid to mention it. As the early draft of the White plan, however, provided this problem in detail and Keynes had a high opinion of its proposal as “an exceeding generous proposed, which would be most helpful to us” (CW, 25, p. 163), the postwar currency scheme and the burden of the large sterling balances were closely interrelated each other. Since discussing such important problem as a whole is beyond this paper, we have to develop the theme in this paper to Keynes’s contribution to the way to deal with the sterling balances and the Anglo-American Financial Agreement.

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