
Instytut Ekonomiki Produkcji
Wydział Ekonomiczny UMCS

Livia FORNACIARI DAVOLI

**Some Issues Concerning the International Monetary Crisis
in the Western System**

Kilka uwag dotyczących międzynarodowego kryzysu monetarnego
w świecie zachodnim

Несколько замечаний о международном монетарном кризисе на Западе

This article refers only to the so-called western monetary system and does not include problems connected with the Rouble area countries. Although the topic considered here is widely discussed nowadays, it still remains one of the most difficult subjects from the technical point of view. In fact, American economists have even invented a new term — the 'stagflation' — to denote the present confused monetary situation, and European specialists talk about 'deflating-inflation' or 'inflating-deflation', with a play on words which is neither clear nor simple. The range of problems is so broad that a more thorough consideration of them in a single paper is impossible. Therefore only some selected issues concerning the problem in hand will be considered in the present paper.

The events which have caused the first collapse in the western monetary system are, in order of time, as follows: the revaluation of the Austrian and Swiss currencies, the decision to let the German mark and the Dutch florin float (May 1971), the declaration of inconvertibility of the American dollar, and the imposition of an extra 10% tax on imports into the United States of America (August 1971).

The financial measures of May 1971 were taken in order to stem the flood, that is, to check the exuberance of dollars on the European market (during the first week of that May the German Bundes-Bank had to absorb over two milliards of dollars, in accordance with the binding pacts of the International Monetary Fund).

These decisions, taken when the agreements concerning the economic and monetary union of Western Europe had just been carried out successfully, and when a good number of proposals had already been agreed upon (such as the reduction of the margins of fluctuation, which should have come into effect from 15 June 1971) ruined all the efforts made so far towards the establishment of the common European currency and they endangered, and certainly delayed, the common agricultural policy.

The second shock in the monetary world was the well-known set of financial measures taken by Nixon on 15 August 1971 in order to recover the economy, and save the dollar. These measures caused such a derangement as to necessitate the urgent reconsideration of the problem of a better organizational structure in the international monetary system, and of a new order in the monetary relations among the members of the international community.

Nixon's dispositions included some points worth repeating here:

1. Declaration of inconvertibility of the dollar into gold, that is, the actual devaluation of the American currency. The dollar had always been the key-money in international exchanges, and together with gold, still forms a good deal of the reserves kept in the treasure-chests of the Central Banks of the Western countries. These reserves have to cover the internal currency, and ensure solvency in the international transactions.

2. Imposition of an extra 10% tax on imports, which created a protective barrier bound to strike hard at European exports, too.

Why did the United States decide to take these grave measures that had to upset the monetary order and, moreover, the international trade? Some of the reasons for such measures shall be mentioned in what follows.

First of all, the gold reserves kept in the famous Fort-Knox were no longer sufficient to cover even one third of the American currency throughout the world. Supposing that the countries and private holders of American money demanded the convertibility according to the international agreements, the United States could cover only a small part of their debt. But still more important is the fact that the American balance of payments has been showing frequent heavy losses for many years (since 1964 or 1965): a constant deficit due to war expenses (especially for the war in Vietnam), to various aids to the underdeveloped countries, and to the investment policy of the United States all over world.

Moreover it is symptomatic that, unlike what happened in the early sixties, the massive deficit of the balance of payments comes not only from a net efflux of capital, but also — and chiefly — from a progressive impairment of the commercial balance, especially if we consider that the standard of the active balance had always been very high in the financial

history of the United States. In short, imports into the United States tended increasingly to exceed exports.¹ During the first half of 1971, and for the first time since 1893, there was even a deficit in the United States balance: a fact also due to lack of competitiveness with the main industrial countries in the field of manufactured goods (particularly Japan West Germany).

All these factors accounted for the crisis, and everybody began to think it might be endless, when suddenly 'coup de theatre': in December 1971 Nixon and Pompidou met in the Azores. Soon after the 'Group of 10'² assembled and ratified a treaty of monetary peace. The United States of America agreed to devalue the dollar, and other currencies were re-aligned.

This peace, however, was only an armed peace, since all the motives that gave rise to the war are still persisting. Thus we are brought back to the thought that the present international monetary system is obsolescent and cannot face its own tasks any more.

It has been said that there was only an armed peace; this is proved by the latest events. First, the English pound crisis, then the new influx of the American deficit and to speculators' activities (during only 5 days of February 1973 more than 10 milliard of dollars were changed into European money, and most of them were coming from the oil royalties). On February 13 the dollar was devalued for the second time. The Italian government immediately let the lira float. In January the lira double market was decided: financial lira and commercial one. In March all European Economic Community currencies, except the Italian lira and the English pound, floated together towards the dollar. In short, a real monetary chaos occurred, and now we must try to consider the consequences and the prospects of the situation.

It is obvious that one can only make conjectures supported by the logic of economics, by the analysis of facts and by the assumption of solution reasonably advantageous for everybody — about the development of the Western monetary system. In fact, it is evident that the political game played by the parties concerned might lead to the most unexpected solutions. One should not forget that the 'crack' in the Western monetary world occurred at a very delicate moment: just when, through Nixon's new policy of 'opening' to the East, the gap between the United States and China was at the point of being actually reduced, and this began to modify the balance of power fixed after the Second World War.

¹ See M. De Luca: *La crisi del dollaro e le prospettive del commercio internazionale*, 'Argomenti', June 1972, p. 337.

² Now 'Group of 20'.

The monetary order cannot depend any longer (hardly anybody sustains the contrary by now)³ on the system of the gold standard as conceived so far, that is, on gold as sovereign for settlement of each country's external accounts. Supposing we wanted to resume this system, we should also have to accept its immediate disagreeable consequence. The gold standard is an extremely mechanical system where, as soon as the gold reserves diminish, the unemployment increases because the volume of currency grows lighter, the prices fall down, and a lot of firms bankrupt. It is inconceivable that any government should be willing to let employment and welfare depend on the eventual discovery of new gold deposits.

Nor can the dollar play its leading role in the international monetary movement any longer. Apart from the present weakness of the dollar, with all risks immanent in the function of the key—money it has always remember that the external accounts of the United States of pound, the dollar has practically been the only reserve money at the Central Banks — there is also a matter of principle: we can no longer accept a system based on a hierarchy of countries, where some (especially the United States) are entitled to make up their external deficiency indefinitely by offering their own national currency, while others are obliged to recover the equilibrium of their payments deficit promptly in case they have drawn on the monetary reserves. Besides, we must always remember that the external accounts of the United States of America get better while those of the other Western industrialized countries get worse. There does not exist any political art capable of making everybody a creditor at the same time. Therefore we have to choose: either we resolve to reduce the American deficit, accepting the consequences of the devaluation of the dollar or we must go on hoarding inconvertible and devalued dollars. In this case the anomalous situation that has given rise to the crisis would deteriorate irremediably, thus adding further damage to a system already too far removed from the principles of rationality and balance that were the objectives of the Brenton Woods agreements. In fact, the crisis is not accountable so much to the system itself as to the constant non-observance of its primary rule, which is the adoption in each country of a national policy capable of removing the unbalance in the external accounts. Therefore the fact that the dollar has taken up the key-position, which was not contemplated at all in the statute of the International Monetary Fund, is not the origin of the crisis. On the contrary, the real reason for the crisis is to be ascribed to the disregard of the rules of the game. However,

³ See L. Levy: *Pourquoi notre système monétaire international passe-t-il par des crises récurrentes?* Lecture to the International Congress CIADEC, Milan 1972.

such state of things was convenient for everybody: for the American debtor, who had an opportunity of settling his net debts through his own national money, and for the others who did not want to bear the consequences of the readjustment in the American trade balance.

At present the prospects for the future are to be considered in the short and in the long run. In the short run we can foresee the system divided into different regional unions: the European area, the Dollar one, the Yen one, and so on. Each of these areas would be arranged in the form of fixed changes inside and floating changes outside. On the other hand, in the long run, there is only one good prospect for the future: the restoration of monetary order through a mechanism where the whole extent of the international means of payment depends neither on the actual stock of gold, nor on the right of a country to impose its national currency upon the world, but rather on the common and conscious will of all countries to act together towards the common goal. This is a general tendency that has emerged from the recent summit conferences, especially from the meetings of the 'Group of 20' of the International Monetary Fund. It calls for the gradual establishment of an international standard dominated by no particular money, no matter how important the issuing country may be. On the grounds of this premise the only possible standard for a stable monetary system will be a method of credit directed by an over-national authority fully alive to the fact that currency is not a commercial instrument, but also a factor deeply conditioning the progress or the regress of the human society.

The famous Special Drawing Rights, ruled by the International Monetary Fund, might already anticipate, at least in part, this solution. They are but credit money issued by the International Monetary Fund and guaranteed by the currencies of many member countries of the International Monetary Fund.⁴ The Italian Minister of Treasury stated in his official report to the Parliament Joint Committee, on 3 September 1971: 'a standard depending on the Special Drawing Rights and on the new principles of parity connected with them is the only possible choice'.⁵ He also quoted the words pronounced in 1967 by the then Minister at the meeting for the adoption of the Special Drawing Rights: 'The Special Drawing Rights, in accordance with the most modern economic conceptions, tend to create monetary liquidity through responsible collective choices, rather than through the floating offer of gold or the unilateral

⁴ M. L. Fornaciari Davoli: *Liquidità ed esigenze di riforma del sistema monetario internazionale*, Parma 1970, chapt. IV.

⁵ See *Dichiarazioni del Ministro del Tesoro*, 'Mondo Economico', September II, 1971, p. 40.

decisions of the reserve-centers. The countries that have been left out of consideration so far, in spite of their growing economic importance, must now take part in the collective decisions'.⁶

On the other hand the Special Drawing Rights, though they might represent a solution to the problem of monetary liquidity, cannot resolve the hard problems of adjustment and equalization: most economists agree upon the priority of adjustment and equalization over liquidity, as a chief factor of international balance. Therefore we must tend towards a solution envisaging the adjustment of the trade balance in each country, particularly in the United States. On this subject I published a monography in which I defended the above position i.e. the priority of adjustment in regard to liquidity. My study ended with the following words:

'As long as we create new means of reserve, we undoubtedly defer the problem of adjustment. Yet today the international monetary system demands no longer wider margins of discretion in delaying any actual solution; it demands a process of adjustment which may serve properly the needs pressing from all sides. Solving this hard problem means either to let the deficiencies annul one another, or to look for new drastic measures capable of attaining the chief aim.'⁷

That is to say, all efforts towards the solution of the monetary crisis will prove useless, if we do not recover soon the essential unbalance at the basis of the different countries deficits, accepting any sacrifice we may be compelled to make — especially in relation to the European exports.

In the course of another report of mine I pointed out the polemic gist of a seminar held in Bruxelles at the same time as the meeting of the International Monetary Fund in September 1972. There the scholars took a stand against those high level monetary operators, who emphasize liquidity (the monetary aspect) and take no care of adjustment (the real aspect).

Everybody has a right to find fault with the economic policy of the United States; furthermore all countries should also concur in determining the American strategy in relation to the investment policy abroad, the aids to underdeveloped countries, and the war expenses. On the other hand Europe cannot pretend to be the third power (the other two being the Union of the Socialist Soviet Republic and the United States of America) in the international economy without bearing a share of weight proportionate to its ambitions.

⁶ See n. 5, p. 37.

⁷ See M. L. Fornaciari Davoli: *Liquidità ed esigenze di riforma...*, quoted, p. 37.

Now we shall take a short look at the Italian economy, to illustrate some of the problems arising from the situation described above.⁸ The Italian experts assert that Italy will draw some advantage from the present state of affairs, because its exports into the United States constitute only 10% of the whole movement, whereas 55% goes to the European countries; quantitatively, therefore, the balance should be in the active. Yet the economic operators fear the probable reduction of that 10%, in a moment so difficult for the Italian economy. Thus they are now trying to get some credit facilities for the fields especially damaged by the devaluation of the dollar (textiles, footwear, non-electrical appliances, cars, tyres etc.⁹). These facilities should include: deductions from the basic taxable income, aiming at rewarding the initiatives which encourage employment, prompt refund of the general export tax; expeditious procedure in granting loans, loans at easy rates; preservation of the banker's credit i.e. a number of tax and credit inducements for the commercial undertakings. Obviously these measures would impose an additional burden on the Italian public budget which is not very sound. This could start off an inflationary process. Moreover, the dollar devaluation affected indirectly the whole Italian export trade, since the international crisis is working its negative effect on all fields of the Italian trade by now. If the monetary instability persists, it will be impossible for the Italian economy to give all fields a proper assistance. Moreover even if those measures were introduced their effect might have been destroyed by other, more efficient foreign economies.

The writer of the present paper believes that the mainstay of the Italian export trade is to be searched for not so much in an easy credit policy, as in a global investment policy affecting positively the general rate of costs, in order to make the production more competitive at all markets. In fact, the chief problem in Italy today is the recovery of investment; a good line of policy should support the internal demand, so as to enable economy to face the heavy pressure of the international market. In spite of what has been done during the last few years, there is a whole market that could largely absorb the increasing internal production. The new law for the South seems to have been introduced with this purpose in mind. But this is the problem of a dualistic economy¹⁰, the discussion of which would go far beyond the limits of the present paper.

⁸ A Deep Analysis of Italian Economy is in S. Lombardini: *Relazione al convegno sull'Economia Italiana*, Perugia, December 1972.

⁹ See Ceres: *L'economia italiana e la crisi monetaria internazionale*, 'Economia del Lavoro', 2—3, 1971, p. 3.

¹⁰ For this topic see M. L. Fornaciari Davoli: *Il problema salariale in un'economia dualistica*, Padova 1963.

BIBLIOGRAPHY

1. Altman L.: *Professor Triffin on International Liquidity and the Role of the Fund*, International Monetary Fund 'Staff Papers' 1961, vol. III.
2. Ammon A.: *Abwertung und Aufwertung oder freie Wechselkursbildung?*, 'Wirtschaftsfragen der Freien Welt', Festschrift für L. Erhard, 1967.
3. Ascheim J.: *Commercial Banks and Financial Intermediaries: Fallacies and Policy Implications*, 'The Journal of Political Economy', February 1959.
4. Bachmann H.: *Das Postulat flexibler Wechsel Kurse*, 'Aussenwirtschaft', vol. 8, December 1953.
5. Balogh T.: *Una società di ineguali*, ed. Einaudi, Torino 1967.
6. Bernstein E. M.: *International Effects of U.S. Economic Policy*, Joint Economic Committee, United States Congress, 2nd Session, Study Paper n. 16, Washington 1960.
7. Bernstein E. M.: *The Problem of International Monetary Reserves Statement*, 'International Payments Imbalances and Need for Strengthening International Financial Arrangements', Hearings before the Committee, the United States Congress, 87th Congress, 1st Session, Washington May 1961.
8. Friedman M.: *The Case for Flexible Exchange Rates*, 'Essays in Positive Economics', Chicago 1953.
9. Furth J. H.: *International Monetary Reform and the Crawling-Peg-Comment* (e riposta sull'argomento di G. W. McKenzie).
10. Johnson H. G.: *The Case for Flexible Exchange Rates*, 1969.
11. Lutz F. A.: *Demonetisierung des Goldes?* 'Neue Zürcher Zeitung', 15 March 1970, Zurigo.
12. Machlup F.: *Concessioni creditizie e assegnazioni di riserve?*, 'Moneta e Credito' 1967, n. 2.
13. Macmillan H.: *Address to the Massachusetts Institute of Technology*, 7 April 1961.
14. McKenzie G. W.: *International Monetary Reform and the Crawling-Peg*, 'Review' of the Federal Reserve Bank of the St. Louis, February 1969.
15. Triffin R.: *La riforma monetaria e il prezzo dell'oro*, ed. Mulino, 1968.
16. Young P.: *The Dollar Standard versus an International Currency*, 'Euromoney', October 1971.

STRESZCZENIE

W artykule autorka roważa szeroko dyskutowane problemy zachodniego systemu monetarnego. Zagadnienia te należą do najtrudniejszych i najpoważniejszych we współczesnej ekonomice rozwiniętych państw kapitalistycznych.

Po przedstawieniu toku wydarzeń od pierwszych objawów kryzysu zachodniego systemu monetarnego w 1971 r., poprzez posunięcia Nixona mające na celu podtrzymanie pozycji dolara aż do pierwszej połowy 1973 r., autorka zwraca uwagę na fakt, że kryzys zachodniego systemu monetarnego przypadł na okres bardzo trudny. Jest to moment rozpoczęcia przez Nixona otwartej polityki w stosunku do Chin, co spowodowało zmiany w równowadze, jaka ustaliła się po II wojnie światowej.

Autorka stwierdza, że nowy porządek w systemie monetarnym nie może oprzeć się ani na systemie „gold standard”, ani na dominacji dolara jako waluty międzynarodowej. Analizując zagadnienia w krótkiej i długiej perspektywie, przewiduje, że:

1) w najbliższym czasie zachodni system monetarny będzie podzielony na obszary: europejski, dolarowy, japoński i inne;

2) w dłuższej perspektywie można przewidywać oparcie zachodniego systemu monetarnego na wspólnym i świadomym działaniu dla osiągnięcia wspólnego celu.

Autorka przeprowadza analizę sytuacji i drogi stopniowej realizacji systemu, w którym stałość systemu nie byłaby oparta na dominującej pozycji waluty jednego kraju.

Artykuł zamykają uwagi na temat sytuacji monetarnej we Włoszech.

РЕЗЮМЕ

В статье рассматриваются широко обсуждаемые в настоящее время проблемы монетарной системы Запада. Эти проблемы принадлежат к одним из наиболее трудных и важных проблем современной экономики развитых капиталистических стран.

После описания хода событий, начиная с первых симптомов кризиса западной монетарной системы в 1971 г., мероприятий Никсона, целью которых было спасение положения доллара, событий первой половины 1973 г., автор обращает внимание на то, что кризис происходил в очень трудный для Запада период. Этот период знаменовался новой политикой Никсона по отношению к Китаю, что вызвало изменения в равновесии сил, которое установилось после II мировой войны.

Автор утверждает, что новый порядок в монетарной системе Запада не может опираться ни на системе „gold standard”, ни на доминировании доллара как международной валюты.

Анализируя все эти проблемы, можно предвидеть следующее:

1. В ближайшее время западная монетарная система будет поделена на следующие области: европейскую, долларовую, японскую и др.

2. В будущем, для того, чтобы достигнуть общую цель, западная монетарная система будет опираться на совместных и сознательных действиях.

Автор анализирует ситуацию и пути постепенной реализации такой системы, в которой ее постоянство не основывалось бы на доминирующем положении валюты одной страны.

В заключение автор делает несколько замечаний на тему монетарной ситуации Италии.

