Principles for Post-War International Economic Cooperation

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At the close of the Second World War, American officials, in concert with their allies in the United Kingdom and elsewhere, set out to remake the machinery of international commerce. They did so not as naive globalists, but as desperate realists – realists who had survived the Great Depression and the second great war of the century. In designing the framework that would govern post-war international economic policy, American leaders and technocrats adhered to a set of essential principles. These principles had emerged from their hard-earned experience during the breakdown of global cooperation in the interwar years and the staggering bloodshed of the war itself. A careful review of the substance of negotiations over the formation of the International Monetary Fund (IMF) and the General Agreement on Tariffs and Trade (GATT), and political communications by US officials in support of those institutions – including essays, speeches, and testimony before Congress – suggests a set of vital and, perhaps, enduring principles that won the day: multilateral coordination, liberalization, mutual benefit-mutual responsibility, and economy = security. To American leaders these principles were abundantly evident. Their task was to persuade their domestic and international peers of the necessity of these principles and to put them into action. Ultimately they created a set of interlocking multilateral institutions to facilitate global commerce and global peace.

1 INTRODUCTION

> 'We cannot prosper unless we are prepared to give practical effect to the principles we hold.' – William Clayton, Assistant Secretary of State, 30 May 1945

At the end of the Second World War the national economies that made up essentially all of the world economy were in shambles, with their factories either devastated by war or converted to the war effort. As a result, mechanisms for producing desired goods and services and exchanging them across borders – both institutions for cooperation as well as transportation networks – had broken down catastrophically before and during the war. American officials, in concert with their allies in the United Kingdom and elsewhere, set out to remake the machinery of

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international commerce. They did so not as naive globalists, but as desperate realists – realists who had survived the Great Depression and the second great war of the century. In designing the framework that would govern post-war international economic policy, American leaders and technocrats adhered to a set of essential principles. These principles had emerged from their hard-earned experience during the breakdown of global cooperation in the interwar years and the staggering bloodshed of the war itself. A careful review of the substance of negotiations over the formation of the International Monetary Fund (IMF) and the General Agreement on Tariffs and Trade (GATT),[1] and political communications by US officials in support of those institutions – including essays, speeches, and testimony before Congress – suggests a set of vital and, perhaps, enduring principles that won the day: multilateral coordination, liberalization, mutual benefit-mutual responsibility, and economy = security. The importance of multilateral policy coordination was evident from a series of failed unilateral policy actions and the formation of inward-focused regional blocs. The importance of liberalization was evident from the vicious cycle of trade barriers, retaliation, and manipulative currency practices, in particular the suspension of currency convertibility. The joint role of mutual benefit and mutual responsibility was evident from the frequent and rapid transmission of both positive and negative economic conditions and policies across national borders. And finally, the important link between economy and security was evident from the way in which fascism and interstate conflict emerged in Europe following the scope and scale of the Great Depression.

There have been many scholarly and popular efforts to assess the post-war economic framework and the negotiations that gave rise to it. Irwin et al. provide an incredibly detailed account of GATT negotiations.[2] Ikenberry has detailed the dual role of national interests and economic theory in shaping Bretton Woods negotiations.[3] Steil focuses on the key roles of John Maynard Keynes and Harry Dexter White at Bretton Woods, and in particular evidence that Harry Dexter White had spied for the Soviets.[4] Kirshner has edited a thorough anthology on

1 I focus here on the International Monetary Fund rather than the two Bretton Woods institutions. The other half of Bretton Woods, the International Bank for Reconstruction and Development, was designed to address a particular – and expected to be temporary – problem associated with the reconstruction of European economies that had been devastated by war. GATT and the Bretton Woods institutions can be viewed as part of a broader post-war institutional program that included the United Nations, the Marshall Plan, NATO and the European Coal and Steel Community, among other efforts.

2 Douglas Irwin, Petros Mavroidis & Alan Sykes, *The Genesis of the GATT* (Cambridge: Cambridge University Press 2009).

3 G. John Ikenberry, *The Political Origins of Bretton Woods*, in *A Retrospective on the Bretton Woods System: Lessons for International Monetary Reform* 155–198 (Barry Eichengreen & Michael Bordo eds, Chicago: University of Chicago Press 1993).

4 Benn Steil, *The Battle of Bretton Woods: John Maynard Keynes, Harry Dexter White, and the Making of a New World Order* (Princeton, NJ: Princeton University Press 2014).

Bretton Woods and GATT.[5] Bretton Woods has received substantially more attention in the literature that GATT. James outlines some of the reasons why Bretton Woods has taken on this almost mythical character.[6] The aim of this article is to document *what* American officials thought about the necessary shape of post-war international economic cooperation and, perhaps more importantly, *why* they thought it. The original contribution here is to treat the negotiations that led to the IMF and GATT, respectively, as part of a common project that was energized by a common set of principles. I identify those principles by analysing and categorizing the views articulated in primary sources, principally the testimonies, essays and speeches of American officials responsible for leading negotiations and shepherding related legislation through Congress. In order to provide necessary context for the experiences of key US officials, the present effort is also part review of interwar economic policies, and part review of prior research on the Bretton Woods and GATT negotiations.

It is also worth a few words to explain what this article is not – it is not an assessment of the effectiveness of these post-war institutions, whether they have lived up to or squandered their awesome legacies, but rather what motivated their creation. Furthermore, it is not an argument that cold, hard self-interest was absent from the debates over the creation of these institutions. Quite the contrary, self-interest was paramount in the negotiations, but it was a broad and forward-looking self-interest as opposed to the narrowly construed, short-term, and ultimately counterproductive self-interest that had taken hold during the interwar years. In describing the State Department's approach to international economic negotiations in 1944, Dean Acheson succinctly captured US interests, '[o]ur own self-interest dictates that we should collaborate with other countries in this endeavor'. The relative strength of the US economy suggests a greater interest, and lower political cost, in US negotiators advocating for a more open international system. However, as Ikenberry importantly argued, US national interest in the post-war world might have corresponded to a number of possible institutional arrangements for managing the global economy, which leaves open a key role for principle and, as Ikenberry emphasized, the growing consensus around Keynesian economics.[7] Similarly, the role of interest and principle in shaping the desired post-war economic institutions does not on its own suggest that compassion or altruism did not play a role. Naturally the awful consequences of the war had engendered some compassion or even altruism on the part of the American leadership and American people, but compassion and altruism were rarely an explicit political motivation for post-war

5 *The Bretton Woods-GATT System: Retrospect and Prospect after Fifty Years* (Orin Kirshner, ed., London: Routledge 1996).
6 Harold James, *The Multiple Contexts of Bretton Woods*, 28 Oxford Rev. Econ. Pol'y 411–430 (2012).
7 Ikenberry, *supra* n. 3, at 155–198.

economic cooperation. Finally, while the principles discussed here ultimately had global reach, the scope of this article is generally restricted to the US perspective.

The rest of this article is organized as follows. The second section discusses the Great Depression and interwar economic policy. The third section discusses the principles that American officials discerned based on their interwar (and war) experience. The fourth section discusses the key features of the IMF and GATT, as originally constructed, and the ways in which the institutions embodied those principles. The fifth section discusses the only significant blind spot that American officials suffered from in their understanding of interwar economic conditions. The sixth section concludes with a discussion of the extent to which the principles that energized post-war negotiations continue to energize international economic cooperation.

2 ECONOMIC CONDITIONS AND POLICY DURING THE INTERWAR YEARS

The economic and financial conditions, and policy mistakes, of the 1920s and 1930s will sound both familiar and foreign, complete with bursting bubbles, bank runs, monetary missteps, debt-deflation, depression, trade tariffs and, finally, desperate foreign exchange experiments. The experience was a formative one for American leaders and technocrats, and their observation and interpretation of interwar economic conditions and policies would exert great influence over their vision for the post-war economic world. Put another way, post-war economic cooperation cannot be understood without extended reference to interwar economic competition and stagnation.

With few exceptions, the roaring 20s featured increasing employment and income, buoyant asset prices and the expansion of bank credit. This was especially true in the United States, where booming farm lending and high agricultural prices reinforced economic confidence. This confidence led the United States, among other nations, to restore the Gold Standard, which had lapsed during the first world war. The Gold Standard was a rigid monetary and exchange rate policy mechanism – every dollar of currency in circulation must be backed, according to a certain ratio, with gold. This ratio also resulted in fixed exchange rates, depending on the relative size of the ratio across countries. The Gold Standard required central banks to maintain sufficient gold reserves and use policy levers, including interest rates and bank reserve requirements, to ensure that the supply of currency did not grow beyond the gold available to back it. In doing so, the Gold Standard also implied that monetary policy was subordinate to other policy goals. Central banks were disciplined by gold convertibility – currency was exchangeable for gold – so a central bank that allowed the money supply grow beyond available gold reserves risked compromising its ability to meet demand for gold and thus losing credibility. As alien as the Gold Standard seems today, it entailed several advantages which were appealing to policymakers at the time. First, the requirement to maintain sufficient gold reserves limited money growth and therefore reduced the risk of hyperinflation, a common and destructive monetary policy ailment of the time period. Second, fixed exchange rates provided stability and predictability that facilitated international commerce. The ratio of gold to currency and the fixed exchange rate provided clear and observable anchors for monetary policy, which helped to establish and maintain the credibility of the monetary regime.

The Gold Standard came with significant – and ultimately catastrophic – disadvantages as well. Exchange rate stability meant sacrificing domestic price stability, and accepting frequent bouts of deflation. Bernanke identified a 'deflationary bias' associated with the Gold Standard in that central bankers were forced reduce the money supply (and hence prices) if gold reserves dwindled, but were not conversely required to expand the money supply if gold reserves increased.[8] In the 1920s countries that accumulated gold, including the United States and France, boomed while others, including the United Kingdom and much of the rest of Europe, were forced to reduce credit in response to gold outflows. The economic expansion in the United States continued. Beginning in 1928, policymakers at the Federal Reserve became concerned about equity market valuations and investor speculation therein, and raised interest rates substantially from 1928 until August 1929. The boom and bubble began to unravel as US equity markets crashed in spectacular fashion in October 1929. Similarly, the farm lending boom came to an end, and declining commodity prices put many farms in financial peril. Because agriculture was a critical sector for bank lending, banks came under stress as well, resulting in a series of regional bank failures and occasional bank runs. Despite an equity market crash, falling prices, and a wave of bank failures, the Federal Reserve continued to de facto tighten monetary policy and acted only haphazardly in its lender-of-last resort role, which might have provided liquidity to troubled banks and ended self-fulfilling bank runs.[9] The Federal Reserve faced a number of legal constraints that prevented it from being able to lend more broadly, including a very narrow set of acceptable collateral. In addition, Federal Reserve officials feared that lending into a depression, when demand for credit was low, would be counterproductive.[10] Finally, instability abroad and demand to convert currency

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8 Ben Bernanke & Harold James, *The Gold Standard, Deflation, and Financial Crisis in the Great Depression: An International Comparison*, in *Financial Markets and Financial Crises* 33–68 (R Glenn Hubbard ed., Chicago, IL: University of Chicago Press 1991).

9 Mark Carlson & David Wheelock, *The Lender of Last Resort: Lessons from the Fed's First 100 Years*, Federal Reserve Bank of St. Louis Working Paper Series # 2012-56B (2012).

10 Michael Bordo & David Wheelock, *The Promise and Performance of the Federal Reserve as Lender of Last Resort 1914–1933*, Federal Reserve Bank of St. Louis Working Paper Series # 2010-36B (2010).

to gold led the Federal Reserve to raise interest rates periodically to preserve gold reserves. This tightening, one of the fundamental policy mistakes of the twentieth century, further exacerbated economic conditions, leading to additional deflation and bank failures. The dual spectre of debt and deflation led to a vicious cycle – deflation increased the real value of nominal debt and other long-term contracts, leading to further defaults and bank failures, which caused further monetary contraction and deflation.[11]

As it is today, the United States was central to the global economy and economic distress here was both mirrored – through similar policy mistakes – and directly transmitted abroad via US policy changes. For example, higher US interest rates attracted capital from abroad – increasing pressure on foreign economies already under stress – and new US trade barriers produced retaliatory measures abroad. In particular, the Hawley–Smoot Tariff Act, passed in June 1930, led to large increases in tariff rates across notable proportion of US imports. This reduced the exports of US trade partners and led to retaliatory trade policy measures abroad in relatively short order.[12] The bubble was bursting on the other side of the Atlantic as well and the deflationary pull of the Gold Standard had exacerbated financial and economic stress in Europe. In particular, the May 1931 failure of Credit-Anstalt, an Austrian bank of with connections throughout Europe, spread financial panic to European financial centres and worsened an already substantial European contraction. As in the United States, the Gold Standard both precipitated and complicated the policy response to the downturn. Countries that, at least initially, remained on the Gold Standard faced substantial balance of payments challenges.[13] Nations with fixed exchange rates – such as the Gold Standard – could not rely on market forces to equilibrate supply and demand for their currency, but instead had to maintain reserves of foreign currency or gold to meet periodic demands to exchange domestic currency, in particular when falling exports reduced foreign currency earnings. Higher US tariffs and lower US demand, among other things, reduced the dollar earnings of US trade partners, and forced foreign importers to convert their own currencies to dollars more frequently. In the face of increasingly urgent demands for dollars or other foreign currency, countries imposed exchange controls (suspended convertibility to foreign currencies, i.e. capital controls), grossly inefficient barter requirements (known as bilateral clearing arrangements) or quantitative import restrictions (quotas) and tariffs, to reduce the demand for foreign currency necessary to pay

11 Irving Fisher, *The Debt-Deflation Theory of Great Depressions*, 1 Econometrica 337–357 (1933).

12 Douglas Irwin, *Peddling Protectionism: Smoot-Hawley and the Great Depression* (Princeton, NJ: Princeton University Press 2011).

13 The balance of payments is collectively the set of international transactions for goods, services and financial assets that determine a country's net demand for foreign currency.

for imports.[14] Other countries that remained on the Gold Standard instead raised interest rates, which supported the exchange rate but induced the same deflationary contractions that afflicted the United States. By 1931, deflation, depression and an increasing variety of trade barriers afflicted the bulk of the global economy.

Between 1931 and 1933 the Gold Standard became unsustainable for an increasing number of countries. The cost of maintaining the Gold Standard now clearly exceeded the benefits of exchange rate stability. The United States left the Gold Standard in 1933, and many other countries followed.[15]Departing the Gold Standard involved countries ending convertibility to gold, reducing interest rates and increasing the money supply, all of which led to substantial capital flight and a large and immediate depreciation of the exchange rate. This process took place in a succession of urgent, disorderly and uncoordinated policies manoeuvers over seven years, from 1929 to 1936, at which point the Gold Standard became essentially defunct. The transmission and progression of these exchange rate changes across countries became known as competitive devaluation, 'devaluation' being the term for the depreciation from a formerly fixed exchange rate, and 'competitive' in the sense that depreciation temporarily improved export competitiveness at the expense of trading partners. As a result, countries felt compelled to match foreign depreciations with their own to maintain export competitiveness and combat depression and deflation at home. Moreover, countries that departed the Gold Standard experienced economic recovery sooner as depreciation supported exports and, more importantly, monetary expansion ended the vicious cycle of debt-deflation.[16] In a very important sense, these recoveries were too little and too late. Depression and trade wars had destroyed every important national economy, reinforcing economic and political nationalism and creating fertile conditions for fascism and war.[17]

3 PRINCIPLES FOR POST-WAR INTERNATIONAL ECONOMIC COOPERATION

In retrospect, we have the greatest insights into the thinking of the American officials, in particular the heads of Cabinet Departments and their immediate subordinate appointees, that spoke repeatedly and persuasively in public support of the proposed international institutions, often through Congressional testimony, but also through speeches and essays. The protagonists, as it were, are Cordell Hull

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14 Barry Eichengreen & Douglas Irwin, *The Slide to Protectionism in the Great Depression: Who Succumbed and Why?*, 70 J. Econ. Hist. 871–897 (2010).

15 *Ibid.*, at 871–897.

16 Ben Bernanke, *The Macroeconomics of the Great Depression: A Comparative Approach*, 27 J. Money, Cred. & Banking 1–28 (1995).

17 Alan de Bromhead, Barry Eichengreen & Kevin H. O'Rourke, *Right Wing Political Extremism in the Great Depression*, University of Oxford Discussion Papers in Economic and Social History #95 (2012).

(Secretary of State, 1933–1944), William Clayton (Assistant Secretary of State, 1944–1946, Under Secretary of State, 1946–1947), Dean Acheson (Assistant Secretary of State, 1941–1945, Under Secretary of State, 1945–1949, Secretary of State 1946–1953), and Henry Morgenthau (Secretary of Treasury, 1934–1945).[18] Armies of technocrats worked beneath them, but we have less insight into their thinking, and their positions did not require them to take public ownership of their policy views.[19] President Roosevelt (1933–1945) gave Secretaries Hull and Morgenthau the freedom to develop, promote and negotiate the framework. President Truman (1945–1953) provided vital continuity after Roosevelt's death, and ultimately signed the laws and proclamations that codified the international agreements for the United States.

In the section below, I summarize and categorize the manifold views of these officials into a discrete set of core principles. They distil the primary motivations for the key characteristics of the economic institutions that ultimately came to govern post-war international cooperation:

Multilateral coordination. *American officials concluded that international economic policies can and should be changed to meet changing circumstances and domestic needs, but those policies and changes should be coordinated with multilateral partners.*

- American officials firmly believed that alternatives to multilateral policy coordination were inferior, including unilateral policy changes, bilateral agreements, and regional economic blocs. The dramatic rise in protectionism and competitive devaluation had been initiated by a series of unilateral manoeuvers (including unilateral moves by the US), greatly tarnishing unilateralism in the minds of American officials. Ikenberry notes that a broader strategic calculus within geopolitical and military circles was also shifting to a more global perspective.[20] And despite great success with bilateral trade deals under the Reciprocal Trade Agreements Act, American officials now believed that this approach was too timid, too piecemeal and too geographically narrow to be successful in the post-war world.[21]

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18 Harry Dexter White, a top official at Treasury, played a key role in the development and negotiation of the Bretton Woods proposals. However, he is also widely believed to have spied for the USSR. Despite his influence on post-war economic institutions, the label 'protagonist' seems inappropriate.

19 This is not to say that we have no insight. Irwin, et al.'s outstanding review of GATT negotiations, e.g. relies on a wealth of personal correspondences, meeting notes and even diary entries of important policy analysts and negotiators. Irwin, Mavroidis & Sykes, *supra* n. 2.

20 Ikenberry, *supra* n. 3, at 155–198.

21 There is an efficiency case to be made of multilateralism as well, in that bilateral and small regional trade agreements may 'divert' trade from lower cost producers to producers that happen to be party to the trade agreement. *See* Pravin Krishna, *Preferential Trade Agreements and the World Trade System:*

- Clayton, before the House Ways and Means Committee in 1945, had this to say about the effects of – unilaterally imposed – Hawley–Smoot: '[t]he United States had on its books the Hawley-Smoot tariff of 1930, in which rates of duty had been raised to the highest levels in our history. Other countries, partly in retaliation for this disastrous blow at their export trade … resorted to higher tariffs and all other paraphernalia of trade restriction which we associate with the economic chaos of the 1930s'.[22]
- In the same testimony, Clayton was similarly wary of regionalism, '[t]here is the way of economic blocs, in which a group of nations which cannot solve their problems by letting the rest of the world in, try to solve them by shutting the rest of the world out … [It] tend[s] in the long run to contract and restrict rather than expand international trade … [and is] contrary to our deepest convictions about the kind of economic order which is most conducive to the preservation of peace'.[23]
- Morgenthau, in an essay in Foreign Affairs also cautioned against creating an exclusive economic club, 'there would seem to be considerable danger – political as well as economic – in setting up a world divided into two blocs. Such a division of the world would not only deprive us of the general advantages of multilateral trade but would inevitably lead to conflict between the two groups. The fact is that the problems considered at Bretton Woods are international problems, common to all countries, that can be dealt with only through broad international cooperation'.[24] In 1944, Acheson emphasized before the House Special Committee on Post-war Economic Policy that '[t]he plan [for the International Monetary Fund] aims toward the establishment of a broad multilateral trading system where trade can expand and its full benefits be realized'.[25]
- In contrast to multilateral proposals, the interwar years were associated with three distinct economic blocs, one associated with the German sphere of influence, a second the growing Japanese empire (known as the Greater East Asia Co-Prosperity Sphere), and third a

A Multilateralist View, in *Globalization in an Age of Crisis: Multilateral Economic Cooperation in the Twenty-First Century* 131–160 (Alan M. Taylor ed., Chicago, IL: University of Chicago Press 2013).

22 William Clayton, *Statement of the Honorable William L. Clayton, Assistant Secretary of State for Economic Affairs*, House Committee on Ways and Means (18 Apr. 1945).

23 *Ibid*.

24 Henry Morgenthau, *Bretton Woods and International Cooperation*, 23 Foreign Aff. 182–194 (1945).

25 Dean Acheson, *Postwar International Economic Problems*, House Special Committee on Post-War Economic Policy and Planning (30 Nov. 1944).

'sterling bloc' associated with the UK and some of its current and former colonies (and shared use of the pound sterling). Moreover, according to Irwin et al.'s account of GATT negotiations, Cordell Hull was convinced that the retreat to regional economic blocs had played a key role in precipitating the war.[26]

Liberalization. *American officials believed that policy should reduce domestic and international barriers to trade and that exchange rate policy should make all currencies freely tradeable (convertible) – these were to be the two major aims of postwar liberalization.*

– To be perfectly clear, these politicians were not laissez-faire capitalists or free trade absolutists. They were by and large 'New Deal' Democrats, and their technocratic staff, who supported free enterprise but also believed that policy should actively intervene to promote full employment and stabilize exchange rates. So it is all the more remarkable that this group came to believe and argue forcefully for an agreement that would reduce an array of tariffs. In arguing for the Reciprocal Trade Agreements Act (RTAA) in 1943, which would provide the legislative authority for the negotiation and ratification of GATT, Hull shared his conclusions about the need for liberalization, '[i]t was clear to us that satisfactory economic recovery was impossible without a restoration and expansion of healthy foreign trade … through a reduction, here and abroad, of unreasonable and excessive trade barriers'.[27] Clayton, also arguing for the RTAA, this time in 1945, said that '[n]o one familiar with the exorbitant rates in the Smoot–Hawley bill, many of them running over 100 percent, can deny that tariff adjustment, selectively and carefully made, is called for'.[28] In 1944, Acheson described the goals of multilateral trade negotiations simply, '[w]e seek … with as many nations as possible … the effective and substantial reduction of all kinds of barriers to trade'.[29] Similarly, a draft proposal issued by the State Department to facilitate discussion and solicit feedback stated, '[t]o seek employment by prohibiting imports … would be harmful and self-defeating'.[30]

26 Irwin, Mavroidis & Sykes, *supra* n. 2.
27 Cordell Hull, *Stable Peace and Economic Warfare Will Not Mix*, House Committee on Ways and Means (12 Apr. 1943).
28 William Clayton, *Statement of the Honorable William L. Clayton, Assistant Secretary of State for Economic Affairs*, Senate Committee on Finance (30 May 1945).
29 Acheson, *supra* n. 25.
30 William Clayton, *Proposals for Expansion of World Trade and Employment* (Washington, D.C.: Department of State 1945).

- More open trade in goods was only one kind of liberalization – free trade in currencies would also be necessary to restore global commerce. Acheson made the case to Congress in 1944 for the crucial role of currency convertibility in international commerce, '[f]oreign investment and financial transactions … require … the assurance that interest and principal can be converted into the lender's own currency … Exporters are not inclined to export unless there is reasonable assurance that they will get paid in money … which can be readily transferred into their own currency'.[31]
- American officials did not offer simplistic and one-sided mercantilist arguments for liberalization. Clayton, for example, explained that, 'a nation profits because it secures better or cheaper goods abroad than at home … [Our trade partners] … produce many things more cheaply than we … which they can sell to our consumers if we permit them to do so'.[32] Even President Roosevelt offered a nuanced argument for the benefits of imports in a posthumous letter to Congress in support of the RTAA, '[i]t is also important to remember that imports mean much more than goods for ultimate consumers. They mean jobs and income at every stage of the processing and distribution channels through which the imports flow to the consumer'.[33]

Economy = Security. *The link between the economy and security had two important components for American officials, (1) robust economies are essential to national and international security, and security is essential to economic stability and growth, and (2) international cooperation in the economic and financial arena was essential to, and must proceed in parallel with, international cooperation in the political and security arena.*

- The latter arena being associated in particular with the United Nations, or as Morgenthau put it in Foreign Affairs, '[i]nternational monetary and financial cooperation is indispensable for the maintenance of economic stability; and economic stability, in turn, is indispensable to the maintenance of political stability. Therefore, a program for international economic cooperation of which Bretton Woods is the first step must accompany the program for political and military security toward which the United Nations are moving. Bretton Woods is the model in the economic sphere of what

31 Acheson, *supra* n. 25.
32 Clayton, *supra* n. 22.
33 Franklin D. Roosevelt, *Message from the President of the United States Urging Extension of the Reciprocal Trade Agreements Program*, House Committee on Ways and Means (26 Mar. 1945).

Dumbarton Oaks is in the political. They reinforce and supplement each other. Political and economic security from aggression are indivisible, and a sound program for peace must achieve both'.[34] In 1943 Hull described the relationship, and virtuous cycle, between peace and economic security, 'it was also clear from the beginning that a revival of world trade was an essential element in the maintenance of world peace … without prosperous trade among nations any foundation for enduring peace becomes precarious and is ultimately destroyed … .The political and social instability caused by economic distress is a fertile breeding ground of agitators and dictators, ready to plunge the peoples over whom they seize control into adventure and war'.[35,36]

– Acheson married these two aspects of economy = security before Congress in 1944, 'Without security, few nations can follow courses which lead to high and rising standards of living. On the other hand, there can be little international security in a world in which the life of the people is unsatisfactory and insecure. This is recognized in the proposals of the Dumbarton Oaks conference, and we need to remember it in our consideration of economic problems.'[37]

Mutual benefit-Mutual responsibility. *American officials believed that international commerce was mutually beneficial – positive-sum, not zero-sum – and that national economies were deeply interdependent. However, harnessing those benefits came with important responsibilities.*

– Officials articulated those mutual benefits in a number of ways, including both straightforward benefits associated with exports, and more subtle benefits associated with cheaper imports and income earned by US trade partners. Morgenthau endorsed the thesis that 'we are an integral part of the world economy and that the relations between the parts and the whole are intimate and mutual. High levels of employment in the United States strengthen economic and political stability throughout the world, which in turn reinforce American domestic prosperity'.[38] Similarly, Hull

34 Morgenthau, *supra* n. 24, at 182–194.
35 Hull, *supra* n. 27.
36 Subsequent research, while subject to some nuance and qualification, has largely borne out Hull's hypothesis, e.g. '[t]here is now extensive social scientific evidence that interdependence … reduce[s] interstate conflict'. *See* Havard Hegre, John Oneal & Bruce Russett, *Trade Does Promote Peace: New Simultaneous Estimates of the Reciprocal Effects of Trade and Conflict*, 47 J. Peace Res. 763–774 (2010).
37 Acheson, *supra* n. 25.
38 Morgenthau, *supra* n. 24, at 182–194.

testified in 1943 that international commerce should be expanded through 'mutually beneficial trade agreements'.[39]

– Mutual benefits and interdependence, however, were not sufficient to sustain international cooperation. A mutual view of responsibility was also required. Three key responsibilities were articulated repeatedly by American officials: (1) reciprocity in the reduction of trade barriers, (2) refraining from devaluation or illiberal currency practices, and (3) increasing and maintaining full domestic employment. US trade policy during the Roosevelt administration was built on a series of reciprocal trade agreements, and this experience informed American negotiators even as they moved to a multilateral context. Nations could join and benefit from a liberal, multilateral trading system only if the their own economies reciprocally opened to exports from trade partners. This was the core rationale for the RTAA. In Hull's words the United States would 'grant to foreign countries reductions in our tariff rates in exchange for benefits to our trade by other countries'.
– Competitive devaluation was of course viewed as a scourge of the interwar years as countries in distress sought to reduce their own exchange rate and export their own unemployment elsewhere. Morgenthau repeatedly rails against competitive devaluation as well as other manipulative currency practices, in particular exchange controls (abrupt suspension of convertibility) and bilateral clearing arrangements (a form of forced barter for particular trade partners or particular commodities).[40] In Foreign Affairs, Morgenthau described these practices as 'measures of international economic aggression' and warned that, absent cooperation 'we may be faced with a resumption and intensification of monetary disorder and economic aggression in the postwar period'.[41]
– If countries could not export their unemployment elsewhere, they would be obliged to use other, less destructive tools to support their own workers. In fact, even more so, nations each had a *responsibility* to expand employment in their own economies, to increase demand for imports (benefiting trade partners) and to help maintain

[39] Hull, *supra* n. 27.

[40] In a striking and perhaps dubious anecdote Morgenthau claims, while testifying for the passage of the Bretton Woods Agreements that 'a movie company was bamboozled into taking a live hippopotamus for its films'. Henry Morgenthau, *Statement of Hon. Henry Morgenthau, Jr., Secretary of the Treasury, Washington, D.C.*, Senate Committee on Banking and Currency (12 June 1945).

[41] Morgenthau, *supra* n. 24, at 182–194.

political support for global integration. A State Department draft proposal prepared by Clayton stated, '[t]he attainment of approximately full employment by the major industrial and trading nations, and its maintenance on a reasonably assured basis, are essential to the expansion of international trade on which the full prosperity of these and other nations depends'.[42] Morgenthau said, in Foreign Affairs, that '[i]t will be incumbent on us to adopt the kind of domestic program which will make possible the attainment and maintenance of high levels of employment with rising standards of living'.[43] Acheson told the House Special Committee on Post-war Policy that other countries would not be keen to join a series of multilateral agreements if they did not believe that the United States, among others, would use serious and constructive means to increase employment '[t]hey will look for some assurance that this country will … maintain a high level of prosperity'.[44]

4 THE IMF AND GATT

The relative strength of the US negotiating position – and a relatively strong degree of consensus between US and UK negotiators – implied that these principles exerted a strong influence on the international economic agreements negotiated during and after the Second World War, namely the Bretton Woods Agreement and the GATT. The size of the American market also made US commitments to liberalization a decisive factor in a broader multilateral agreement – US trading partners were willing to engineer substantial opening of their own economies, for the US and other countries, to gain access to the US market. The Bretton Woods Agreement encompassed the Articles of Agreement for the International Monetary Fund as well as the Articles of Agreement for the International Bank for Reconstruction and Development (to become the World Bank). There were forty-four members, initially, of the Bretton Woods Agreement. The GATT began with twenty-three members.

The IMF had four essential features. First, member exchange rates were fixed within relatively narrow bands in the short term. Second, member exchange rates were allowed greater flexibility over the medium term. However, consistent with views on the importance of multilateral policy coordination, repeated and large exchange rate changes required consultation with and approval by the IMF Board.

[42] Clayton, *supra* n. 30.
[43] Morgenthau, *supra* n. 24, at182–194.
[44] Acheson, *supra* n. 25.

Third, member currencies must be fully convertible and on a non-discriminatory basis – domestic currency could be exchanged for foreign currency without restriction. For negotiators, this was an essential aspect of post-war liberalization. Fourth, and perhaps most innovative, members pooled resources and committed to supply their own hard currency to members with temporary balance of payments difficulties. That is, countries that committed to stability and convertibility for their own currencies would have access to foreign currency should idiosyncratic events lead to a temporary drop in exports, for example. This provided an alternative to more draconian strategies for managing balance of payments challenges, like the exchange controls or quantitative import restrictions that were common during the interwar years. Long term exchange rate flexibility was also intended to address the rigidity of the Gold Standard, which was valued for making international trade more predictable but also viewed as inflexible in the face of the exceptional economic headwinds of financial panics and deflation.

First and foremost, the GATT substantially reduced tariffs for all multilateral participants.[45] In this way GATT straightforwardly embodied the principles of both multilateral coordination and liberalization. GATT also established several important rules of the road for international trade and would serve as a permanent framework for future 'rounds' of trade liberalization and rulemaking. For example, GATT outlined the conditions under which members could temporarily protect domestic industries, for example due an unexpected surge in imports or from foreign subsidies, or use quotas to address balance of payments difficulties. The agreement enshrined the multilateral principles of 'most favored nation' (any tariff reductions negotiated with one partner would automatically extend to all members), and 'national treatment' (all legislative and regulatory product requirements would apply to both domestic and foreign goods equivalently).

Both institutions were considerably less ambitious than alternative proposals that had advanced well into real negotiations. Earlier and competing visions for the IMF included provisions for a larger pool of liquidity (which would have enhanced the insurance function), and the ability to issue its own currency to serve as an international unit of account and alternative reserve asset to gold and the dollar.[46] Issuing its own currency would have also provided a more flexible and potentially larger liquidity pool to offer members experiencing balance of payments challenges. In the end, these proposals raised concerns about rewarding poor macroeconomic behaviour (moral hazard), with Americans coming out in favour of somewhat less ambitious visions.[47] In addition, GATT was intended as

[45] Irwin, Mavroidis & Sykes, *supra* n. 2.
[46] John H. Williams, *Currency Stabilization: The Keynes and White Plans*, 21 Foreign Aff. 645–658 (1943).
[47] Ikenberry, *supra* n. 3, at 155–198.

a mere precursor to a more sweeping International Trade Organization (ITO) with a permanent staff, and a scope that would encompass almost every aspect of domestic and international commerce. The ITO was intended to govern, and to some extent unwind, non-tariff barriers, export subsidies, cartels, and 'state trading' or state-owned enterprises.[48] The GATT was ratified just as momentum left ITO negotiations and governments became more domestically focused, immediately following the cessation of hostilities. The UK also lobbied successfully for substantial deviations from non-discrimination in order to maintain its imperial preferences, a system of reduced trade barriers for British colonies. Such preferential access was inconsistent with multilateral most favoured nation treatment but was too much a part of UK political identity to be dislodged, despite years of US efforts during the negotiations.[49]

5 THE LIMITS OF EXPERIENCE: THE GOLD STANDARD AND MONETARY POLICY

It would be both wrong and naive to regard our political ancestors as having attained a perfect enlightenment and absolute omniscience. Their accounting of the policy mistakes of the interwar years was incomplete – they did not fully understand the role of the Gold Standard in facilitating and deepening the Great Depression, or the role of the abandonment of the standard in promoting recovery. In their zeal for the stability of the pre-war years, nations forgot even the modest flexibility allowed by the IMF, opting instead for permanently fixed exchange rates. This fixed exchange rate system lasted until 1971, barely more than twenty years, when the United States broke its own commitment to gold convertibility that was the anchor for the global system of fixed exchange rates. What little flexibility that had been envisioned in 1945 was forgotten, and the rigid exchange rate arrangements that remained were insufficient to weather changing economic circumstances and shifting balance of payments needs. IMF negotiators had recognized that the interwar Gold Standard had yielded unsustainable exchange rates, but were confident that a *different* set of more or less fixed exchange rates would prove sustainable and would provide the predictability required by internationally active firms.

Multiple threads of research on monetary policy around the Great Depression tell a very different story than the one IMF negotiators told each other. In particular, three critical research results upend this post-war consensus. First,

[48] Clair Wilcox, *The London Draft of a Charter for an International Trade Organization*, 37 Am. Econ. Rev. 529–541 (1947).

[49] Irwin, Mavroidis & Sykes, *supra* n. 2.

Romer found that monetary policy was almost entirely responsible for the US recovery from the Great Depression. At the time, American officials were invested, both politically and psychologically, in the success of the New Deal's aggressive fiscal expansion and employment policies.[50] Second, Bernanke found that countries that left the Gold Standard experienced almost immediate economic recovery, while their peers remained in deflation and depression.[51] American officials recognized the need to leave the Gold Standard in 1931, but associated leaving the standard with disorderly currency markets and competitive devaluation. Third, Eichengreen and Sachs have the final piece of the puzzle. While competitive devaluation was viewed as zero sum in the post-war consensus, Eichengreen and Sachs found that devaluation was positive sum, in fact greatly so, once all major economies had devalued.[52] This is entirely consistent with Bernanke's findings. In essence the problem was one of disorderly and competitive devaluation, rather than coordinated and cooperative devaluation. One can arguably read the IMF Articles of Agreements as consistent with this view, but members never fully utilized the coordination mechanisms or the flexibility allowed to orchestrate, for example, substantial and simultaneous monetary policy changes across many countries.

6 CONCLUSION

As the formation of the post-war international economic order becomes more distant in time, its rationale is at risk of becoming similarly remote. Over time, the economic damage of the interwar period became less salient. The political arguments for multilateral global trade changed, and in many ways became weaker. Political defences of globalization and trade agreements quickly became uninspired. By 1954, the periodic renewal of US legislation necessary for trade negotiations no longer referenced national security considerations.[53] Over time, proponents of more open trade emphasized mercantilist, export-oriented gains and under-emphasized distributional effects. Instead, arguments for deepening international linkages took for granted that sufficiently broad-based gains would result from increased trade and capital flows. Rodrik has argued persuasively over a large body of work that the rhetorical defence of globalization and multilateral institutions had become simplistic and unconvincing.[54] And a similarly simplistic implementation

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[50] Christina Romer, *What Ended the Great Depression?*, 52 J. Econ. Hist. 757–784 (1992).

[51] Bernanke, *supra* n. 16, at 1–28.

[52] Barry Eichengreen & Jeffrey Sachs, *Exchange Rates and Economic Recovery in the 1930s*, 45 J. Econ. Hist. 925–946 (1985).

[53] Raymond Vernon, *Foreign Trade and National Defense*, 34 Foreign Aff. 77–88 (1955).

[54] E.g. Dani Rodrik, *The Globalization Paradox: Democracy and the Future of the World Economy* (New York: W. W. Norton & Company 2011).

of globalization had not delivered results. Weak arguments and inattentive implementation have both served to undermine the legitimacy of globalization and the international institutions that set many of the global rules of the road.

Colgan and Keohane take the argument a step farther. They argue that the liberal international order, another term for the institutions that arose out of the Second World War, is 'rigged' and the working class has been ill served by a zealous devotion to this order and its institutions.[55] Colgan and Keohane rightly highlight the need for better employment policies and a renewed social contract in restoring support for the order, but they fail to acknowledge that as conceived, domestic responsibility for full employment was a *core feature* of the order. The liberal international order was conceived with the Great Depression in mind. Better to say that the liberal international order has been forgotten than to argue that it has failed. Hull, Acheson, Clayton and Morgenthau implored their domestic and international peers to focus on increasing employment. According to their understanding of interdependence, higher employment would boost demand for imports, support for openness, the economies of trading partners and global political stability.

Secretary of State Cordell Hull seemed to have an appreciation of the tenuous nature of progress and the fragility of post-war economic wisdom. Progress was not inevitable, but would require commitment and vigilance. He expressed that sentiment in his letter to the Nobel Committee upon receiving the Nobel Peace Prize in 1945, mostly for work related to the founding of the United Nations, in this way, '[t]he crucial test for men and for nations today is whether or not they have suffered enough, and have learned enough, to put aside suspicion, prejudice and short-run and narrowly conceived interests and to unite in furtherance of their greatest common interest'.

One can view each of the four principles as necessary parts of a whole – the edifice of international economic cooperation crumbles without a holistic approach. One cannot organize international economic policy, for example, around mutual benefit without mutual responsibility, or based on unilateral policy changes and (imagined) foreign acquiescence. Moreover, one cannot promote international security without liberalization, or increase liberalization without full employment. Ironically, American officials in the 1940s, as well as like-minded Keynesians, had a deeper understanding of the centrality of full employment to global integration than their predecessors, while leaving fewer tools to address it. Fixed exchange rates made it more difficult to use monetary policy to support employment. In the Eurozone the problem is even more acute, with both

[55] Jeff Colgan & Robert Keohane, *The Liberal Order Is Rigged: Fix it Now or Watch it Wither*, 96 Foreign Aff. 36–44 (2017).

monetary and fiscal policy under external constraint. Even unshackled monetary policy in the United States found it difficult to increase employment after the 2008 financial crisis. A more robust and full spectrum policy response would be necessary to ensure employment remains high enough to support continued global engagement. Failing to do so entails substantial risk. Protectionist economic nationalism was not a theoretical abstraction for American political leadership of the 1940s, it was a tried and failed economic and political strategy. American attempts at helping particular sectors via the Hawley–Smoot tariffs were met with retaliation abroad and reduced trade in both imports and exports. When combined with deflation and depression, this economic strategy reinforced isolationist and fascist politics in Europe. American leaders envisioned an alternative based on interdependence, mutual responsibility and shared security and prosperity. Policymakers need not repeat their experiences to learn from them.

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