forward more than 20 percent to 890 since the low of last Febuary. . . .

What is puzzling at first sight is that the rise should have taken place when the consensus of economic opinion is... that the United States is now headed for contraction as the government takes action to curb inflation. . . .

Financial Times, *Aug. 18 article by Samuel Brittan: "Myths About Exchange Rates":*

Seven years ago I was recalled from holiday because President Nixon had suspended the convertibility of dollars into gold and imposed an import surcharge — as well as imposing wage and price controls. The parallels are ominous. It is August and the dollar is again under pressure, the U.S. President has asked for top level studies, and the weekend after next I shall be passing through Salzbourg — the place from which I was recalled in 1971. This time the main cause for worry is not the falling dollar, but the supposed remedies for it — whether central bankers and central planners share a common distaste for exchange rate movements, as do the businessmen who would like stable exchange rates in an unstable and inflationary world. As a result of these prejudices (i.e., for fixed exchange rates), and a certain misinterpretation of economic research and teaching, it has become fashionable to say that (floating) exchange rates don't work. This still seems to me an attitude devoid of all merit, and a thought which could do untold damage to world trade.

EMS Negotiations At A Crossroad

British efforts aim at creating antidollar 'parallel currency'

INTERNATIONAL FINANCE

Britain made no bones about its opposition to the creation of a new European monetary arrangement as outlined at the July 6-7 European Community summit meeting in Bremen, West Germany. Now London, together with its customary allies in the Belgian government, is attempting to skew the European Monetary System (EMS) from inside the negotiations, toward deployment of an antidollar "parallel currency."

What is at stake is the character and purpose of the new European Monetary Fund (EMF). Both the final communique at Bremen and statements at the time by West German Chancellor Schmidt blueprinted a two-part fund. The first part would be a pool of European currencies to be used for coordinated intervention in the foreign exchange markets on behalf of the dollar.

The second, a pool of 20 percent of each member's dollar and gold reserves, would involve the creation of European Currency Units (ECUs), which member central banks could hold. Its key features, however, are (1) a de facto remonetization of gold, as acknowledged by both the advocates and opponents of such a move, and (2) the possibility of redeploying foreign-held dollars — augmented by cooperation with the Arabs — in the form of long-term, low-interest development credits to less-developed countries and the socialist sector.

These dollars would in good measure flow back to the U.S. as payments for industrial and technological exports, reversing the U.S. current accounts deficit and decisively expanding the volume of hard-commodity trade volume conducted in dollars, thus securing and indeed upgrading the dollar's reserve-currency status.

This potential was underlined at the time of Bremen by the leading West German business daily *Handelsblatt*, which foresaw the European Monetary Fund issuing long-term gold-backed dollar -denominated bonds to expand its own lending base. The French equivalent of the *Wall Street Journal, Les Echos*, described the fund as *un avaleur des dollars*, a dollar-swallower which to be effective must go beyond central bank-style clearing operations.

Tolerating the British

Thus far, however, the French and West German architects of the fund have to all appearances allowed their conception of the EMS as a seed-crystal for a new development-geared world monetary system to remain the guiding light of a small policy making stratum at the top. The negotiations appear to be afflicted by subordinates' tendency to act as if the EMS were chiefly an affair of the European Community, and to parley with the British as simply another, if troublesome, member of the EC instead of a self-proclaimed saboteur of the dollar and of global industrialization. This state of affairs in turn disorients those in the U.S. seeking genuine dollar support.

West German Finance Minister Hans Matthoefer's Aug. 10 interview with the Bonn *General-Anzeiger* is a case in point. Played down nationally and internationally, the interview was closely read in Bonn and other capitals. Matthoefer's inability to stress the dollar-lending potential of the EMS left him portraying it as a European "bloc." From that point of view, it was naturally difficult to explain how the EMS will help the dollar — since everyone knows that currency intervention, whatever its scale, will not suffice.

Within a European Community framework, Matthoefer portrayed the fund's lending in national currencies, not dollars. The purpose seemed to be to bolster weak European members (like Italy — and Britain?) within the "bloc," rather than to create and sustain international trading and investment partners through centralized loans to the East bloc and Third World.

...And the IMF

Bracketing his polite remarks about the IMF and World Bank, Matthoefer's remarks on European Currency Units were coherent with the IMF's hope of making a European basket-of-currencies-unit into a sort of Special Drawing Right which would encourage central banks to divest their dollar holdings through "substitution accounts." Thus it is a half truth to say, like Bundesbank president Otmar Emminger, that "the devil is in the details." Once the *overall* conception is snarled, the British hope, they can encourage wrangling on technical questions to stall the fund's implementation and foster chaos-and-confusion blows against the dollar. Then they can finally accept a fund version with which they will be glad to live in the absence of dollar-recycling commitments. Matthoefer's emphasis on central bank autonomy and separate interventions reflects a willingness to mollify the British on a deeper question — joint deployment of European resources for gold-backed dollar credits.

An Aug. 15 op-ed by the British delegate to the IMF's executive directorate, William Ryrie, shows the trap from the other direction. Ryrie chats about "details" — such as whether West Germany would force the UK to put its domestic economy in order — while treating the whole EMS question as a matter of currency stabilization. What is unspoken, except in Ryrie's disappointment at the refusal of the U.S. to widen the role of SDRs, is the premise that the EMS will help permanently demote the dollar.

Stoltenberg: Fund Crucial to EC

Under these circumstances it was sensible of Gerhard Stoltenberg, Christian Democratic governor of the West German state of Schleswig-Holstein, an opposition leader and a key industrial spokesman, to propose that the discussion of the EMS be removed from the clouded sphere of Finance Ministers, EC functionaries and central bankers. According to the Aug. 16 *Frankfurter Allgemeine Zeitung*, Stoltenberg stated that questions concerning the system cannot be handled behind closed doors, since the EMS is the most important decision for the European Community since its founding. Stoltenberg challenged Bundesbank president Emminger to publicly state his reservations, if he has any. Over the past five weeks Emminger has informally allied with Christian Social Union demagogue Franz-Josef Strauss and Free Democratic Economics Minister Otto Graf von Lambsdorff to restrict or unhinge the EMS.

—Susan Johnson

Matthoefer: Miscasting EMS As a "European Bloc"

Excerpts from interview with West German Finance Minister Hans Matthoefer, **Bonner General-Anzeiger,** ***Aug. 10.***

On the European Monetary System:

...Reserves will be deposited in a common fund. The balancing of assets and liabilities among the central banks will no longer take place mainly in dollars, as is the case with the "snake," but in European Currency Units (ECUs). This offsets the transfer of reserves from the funds to the central bank(s)...The fund issues credits in ECUs against gold and dollar deposits. A central bank can then use the ECUs to balance those of its obligations arising from (currency-market) interventions.

In addition, a second European Monetary Fund pool will be created through deposits of national currencies. This second pool of funds exclusively serves credit purposes, and the credits will be linked to investment that promotes stability, with the size and term of the credit geared accordingly.

The new monetary system — in conjunction with the second pool's investments — commits us to a strengthening of economic interrelationships and mutual exchanges, a better grounding in a common division of labor, and thus positive effects on our economic growth....

Q: Public discussion indicates many further difficulties and problems... what are the details?

A: For one thing, the definition of the ECU as a common denominator for the upper and lower central bank intervention points....A second group of problems has to do with the targeting of parities vis-à-vis non-fund countries, for instance the dollar or the yen. In a third sphere there arise questions concerning the deposit of reserves proposed at Bremen, and the creation of ECUs as a corresponding offset. A further significant point for the status of the entire system is the policy that must be carried out by countries with varying payments balances in order to effect greater internal and external stability....Certainly speculation against certain national currencies will not come to an end. But it will be far more difficult to speculate against a currency supported within a European Monetary System....

Q: What about fears that national central banks' independence would be adversely influenced?

A: Naturally this will be worked out in the course of settling the details. I do not believe that the

Bundesbank could agree to a set of regulations that diminished its autonomy and compelled it to undertake a liquidity policy that would lead to undesirable price increases.

The upshot is that the existence of independent central banks ought not to be infringed upon; they have to maintain their control over money-supply policy in order to be independent. The Bremen resolution projects this. The interventions will not be carried out by the fund itself, but through the national central banks.

Q: Then there is the question of the EMS's relation to the IMF and the World Bank, which the Americans in particular are concerned about.

A: We are interested in a strong IMF and a strong World Bank and don't want to weaken them through the EMS. The IMF is to retain its important function in administering relations among major currency blocs and the totality of its member states.

Q: The (European Community) heads of state expressed the view that the new system would strengthen the dollar. From the American side there are somewhat contrary fears.

A: We have discussed this at length with the Americans. Since we ourselves are uncertain exactly how, for example, the ECU will be accounted or how intervention will take place vis-à-vis non-member countries, we naturally couldn't assuage the Americans' fears on particular points. However, we are firmly determined not to weaken the dollar, because we have a stake in a strong dollar....We Germans have certainly experienced how the dollar's depreciation has the side effect of enormous export problems for us....The system can lift certain burdens from the dollar. For example, the 'snake' interventions sometimes took place in dollars, but this will now occur instead in European Community currencies. At the same time, the policy of the European currency bloc members vis-à-vis the dollar would certainly be characterized by greater stability....

IMF Spokesmen: "The Devil is in the Detail"

Excerpts from "Powerful Political Impulse Spurs Monetary Integration," Journal of Commerce, *Aug. 15, by William S. Ryrie, UK executive director of the International Monetary Fund and World Bank, and economic minister in the British Embassy in Washington.*

....The great question about the proposals for monetary integration in Europe is whether a system can be produced which is both politically acceptable and economically workable.

As Otmar Emminger, the president of the German Bundesbank, likes to say: "The devil is in the detail." Most of the questions which people have about the new system cannot be answered until the details are settled; and these technical problems are certainly difficult....

It is true that if the new system were set up in a manner which made the other currencies in Europe, in effect, satellites of the German mark, it would be unworkable....Those who are working on it are well aware of these problems and there is no reason to suppose that they will not succeed....

Excerpts from an interview with Roger de Beckker, technical assistant to the IMF executive director for Belgium and Austria, Aug. 14:

Q: Are there plans to use the EMF to introduce a substitution account system as the IMF wanted to do, supplanting dollars with SDR's as reserves?

A: Yes, that's the idea, but I can't tell you if it will happen; everything is still vague and tentative. Negotiations are going on now with the British. The idea is that the EMF would create ECU's against the gold and dollar reserves, then use them to buy up dollars as in an SDR substitution account.

The problem with the ECU is that there is no market in them, so the EMF would use them to buy dollars from central banks or currencies for intervention purposes. There are continual meetings; no one knows how they will turn out.

Q: We have been told that Giscard d'Estaing has moved up the deadline for the EMF arrangements to September.

A: That's true, but I don't believe it will be met. There are too many technical details to be worked out with the British.

Think Tanker: Brits Steering EMF From Within

Comment by think-tank specialist connected with London and Brussels banking and British oil interests, Aug. 16:

Nothing is settled yet about the European Monetary Fund. Everyone is still jockeying. The British are pretending they want to join in order to shape the discussion. They don't want to lose any advantage they might gain by getting in on the negotiations.

A leading official of the West German Finance Ministry commented on Aug. 17:

Of course the British want to smash the dollar and the EMF because they are afraid that London as a banking center will decline if the EMF is implemented. But I don't think Her Majesty's banking system has the strength of pulling this operation this time around.