1944 and after: Concerning the founding of the Bretton Woods' Institutionsr

Series : 70 years since Bretton Woods, the World Bank and the IMF (Part 1)

Thursday 31 July 2014, by TOUSSAINT Éric (Date first published: 15 July 2014).

70 years ago, the 22nd of July 1944, the United Nations Monetary and Financial Conference, better known as the Bretton Woods [1] Conference, that had lasted for three weeks, reached a conclusion. It was attended by representatives from 44 countries [2].

In order to prevent a recurrence of economic crises like the crash of 1929, but also to ensure world leadership in the post-war era, the United States government began to plan for the creation of international financial institutions as early as 1941. The World Bank and the International Monetary Fund saw the light of day at the Bretton Woods Conference of 1944 held in Bretton Woods, New Hampshire. Initially, the Roosevelt administration was in favour of creating strong institutions capable of imposing rules on the private financial sector, including Wall Street. But noticing the hostility of the banking world Roosevelt backed down. Indeed, the distribution of votes within the World Bank and the International Monetary Fund clearly illustrates the will of certain major powers to exert domination over the rest of the world.

In the beginning [3]

It was in 1941, the year the United States entered the Second World War, that discussions were initiated concerning the international institutions to be set up once this major conflict was over. In May 1942, Harry White, chief international economist at the U.S. Treasury, presented Franklin Roosevelt with a blueprint entitled "*Plan for a United and Associated Nations Stabilization Fund and a Bank for Reconstruction and Development of the United Nations*". One of its objectives was to convince the allied nations currently at war with the Axis powers (Germany, Italy, Japan) that once peace was established, certain systems would need to be adopted to prevent the world economy entering a depression similar to that of the 1930's.

Between 1941 and July 1944, when the Bretton Woods Conference assembled, several of the proposals contained in the initial plan were abandoned. But one of them came to fruition: the creation of the IMF (International Monetary Fund) and the IBRD (International Bank for Reconstruction and Development), better known as the World Bank.

To fully understand the roles attributed to these two institutions, we must go back to the late 1920s and the 1930s. The severe economic depression that gripped the United States during this period had a profound effect on world capitalism in general. One of the consequences was that in 1931 Germany stopped repayment of its war debt to France, Belgium, Italy and Great Britain. In a domino effect, these countries stopped repayment of their external debt to the United States [4]. As for the United States, it drastically reduced capital exports in 1928 and even more so in 1931 [5]. At the same time, it cut down on imports. The result was that the flow of dollars from the United States to the rest of the world dried up, and countries with debts to the world's leading power did not have the dollars to pay it back. Nor did they have the dollars they needed to buy North American products. The machinery of world capitalism was grinding to a halt. Competitive devaluations ensued as each country attempted to win market share at the expense of the others. The developed capitalist world was caught in a downward spiral.

In 1932 John Maynard Keynes made this ironic remark about the attitude of the United States: "*The rest of the world owes them money. They will not take payment in goods; they will not take it in bonds; they have already all the gold there is. The puzzle which they have set to the rest of the world admits logically of only one solution, namely, that some way must be found of doing without their exports*" [6].

One of the conclusions drawn by the United States government under Franklin Roosevelt (U.S. President from 1933 to 1945), was that a great creditor nation must make currency available to debtor countries to be used for repayment of their debt. Another, bolder conclusion was that in certain cases, it is preferable to offer donations instead of loans if a State wants its exporting industries to gain maximum and lasting profit. This question will be dealt with in a following article devoted to the Marshall Plan for the reconstruction of Europe (1948-1951).

Let us take a closer look at the Thirties before going on to the creation of the Bretton Woods institutions during the Second World War.

Creation of the Export-Import Bank of Washington (1934)

The Export-Import Bank of Washington (the U.S. public agency for export credit, later called Eximbank) was created in 1934 to protect and promote U.S. exporters. It guaranteed U.S.exports and at the same time granted long-term credit to foreign buyers for the purchase of U.S. goods and services. Each dollar lent had to be spent on merchandise produced in the United States. The Export-Import Bank released funds only on receipt of proof of shipment of goods abroad. At the start, the total amount of loans granted by the Export-Import Bank was a very modest one: 60 million dollars in the first five years. But the volume of loans increased rapidly from then on. In 1940, the Bank's lending capacity was 200 million dollars, and in 1945 it had reached 3,500 million. During its first years of operation, the Export-Import Bank targetted Latin America and the Caribbean, China and Finland, a reflection not only of the economic but also the geo-strategic interests at stake.

The creation of the Inter-American Bank (1940)

In 1940 another financial instrument was created: the Inter-American Bank. This was an inter-state bank founded on U.S. initiative in the context of the Pan-American Union (the ancestor of the Organization of American States (OAS). The original members included: Bolivia, Brazil, the Dominican Republic, Ecuador, Mexico, Nicaragua, Paraguay and the United States. In some respects this bank was the forerunner of the World Bank, which came into being four years later.

The main architect on the U.S. side was a fervent partisan of public intervention in the economy, an advocate of the New Deal: Emilio Collado, no. 2 in the Department of State [7]. He played a prominent role in the discussions leading up to the Bretton Woods conference and in 1944 was appointed US first executive director of the World Bank. The Department of State was not the only player involved in the launch of the Inter-American Bank in 1940. The U.S. Treasury was also represented in the persons of Henry Morgenthau and his assistant Harry White.

Four basic reasons led the Roosevelt administration to approve the creation of the Inter-American Bank.

First, the government realized that it must not only lend money to foreign buyers of U.S. products, but that it must also buy exports from those to whom it wished to sell its goods. Nazi Germany, with its dominance over part of Europe, was in the process of buying goods from, and investing in, Latin America [8]. The establishment of the Inter-American Bank would tighten the bonds between the United States and all its Southern neighbours.

Second, Washington considered that it could not count on the U.S. private financial sector to lend capital to countries south of the Rio Grande when fourteen Latin American countries were in partial or total default on payment of their external debt. In Washington's view, the big U.S. banks were responsible for the 1929 crisis and its continuing effects. The creation of a public agency would enable the government to take serious action.

Third, to convince the governments of Latin America to actively engage in reinforced relations with the United States, they must be offered an instrument which, officially at least, pursued objectives not directly answerable to the United States.

A.A. Berle, deputy secretary of the Department of State, put it plainly: "*In the past, movements of capital have been regarded as, frankly, imperialist. They usually led later to difficulties of one sort and another. The other country did not like to pay; the interests built up were frequently supposed to be tyrannous. We are still liquidating many of the nineteenth-century messes which were occasioned by the somewhat violent and not too enlightened moves of capital*" [9].

Fourth, a bank had to be set up in which the borrowing countries played a part and had a voice. The reasoning was very simple: if borrowers were to repay their debts, they had better be part of the Bank. The same principle was applied when planning the creation of the World Bank and the IMF.

As regards the distribution of votes within the Inter-American Bank, the criteria used were subsequently to be adopted by the World Bank and the IMF. The "one country, one vote" principle was rejected in favour of a voting system based on the economic weight of a country (in this case, export volume).

The system implied an extra bonus for Latin-American countries: the existence of a multilateral banking institution would protect them from strong-arm tactics on the part of creditors anxious to recover their funds. After all, it was not so very long ago that the United States and other powerful creditors had recourse either to military intervention, or to direct control on customs and tax administration of indebted countries in order to recover what they claimed as their due [10].

It should be noted that the firm attitude of a large number of Latin American countries (fourteen in all, including Brazil, Mexico, Colombia, Chile, Peru and Bolivia), which had decided to discontinue, either totally or partially, repayment of their external debt, scored a resounding victory. Three positive results ensued: their economic growth was higher than in countries that continued to repay the debt; they won back a significant degree of autonomy vis-à-vis the rich countries ; far from being excluded from sources of financing, they were wooed by various governments in the North eager to offer them public financing. An instructive lesson in the advantages of standing one's ground.

Discussions within the Roosevelt administration

As of 1942, the Roosevelt administration pursued discussions concerning the economic and financial order to be established after the War. A number of ideas were regularly tabled on the subject of debt and capital movements: it was considered advisable to set up a number of public, multilateral institutions which, to counteract the risky nature of private international investments, would provide public capital. These institutions should "*police international investment by private capital, so as to* *provide judicial and arbitral facilities for settlements of disputes between creditor and debtor, and to remove the danger of the use by creditor countries of their claims as a basis for illegitimate political or military or economic demands.*" (Excerpt from a memorandum of the Council on Foreign Relations dated 1 April 1942).

An ambitious project proposed by Harry White

As mentioned above, in 1941 Harry White at the Treasury was already preparing the groundwork for a plan to set up two major multilateral institutions. Franklin Roosevelt received a first draft in May 1942 based on the premise that before the War ended, it would be necessary to set up an Exchange Rate Stabilization Fund (the future International Monetary Fund) and an international Bank to provide capital. He explained: "Two separate, though linked agencies would be better than one, since one agency dealing with both tasks would have too much power and would run the risk of greater errors of judgment" [11]. The Fund and the Bank would bring together all nations, starting with the Allies. The relative weight of each member nation would be a function of its economic weight. Borrower countries would belong to the Bank, as this would motivate them to repay their loans. The two institutions would favour policies designed to ensure full employment.

The Fund would work to stabilize exchange rates, bring about a gradual discontinuance of exchange controls and the end of export subsidies.

As for the Bank, it would provide capital for the reconstruction of the countries affected by the War and for the development of backward regions; it would help stabilize commodity prices. The Bank would lend money from its own capital and have its own currency: the *unitas.*

Harry White's ambitious project was drastically cut down to size in the years to come. Wall Street and the Republican Party were particularly hostile to several fundamental aspects of the White plan. They wanted nothing to do with two strong public institutions designed to regulate the flow of private capital, and which would in fact be in competition with them. Franklin Roosevelt decided to come to terms with them, with the result that in 1945, Congress eventually ratified, by a large majority, the Bretton Woods agreements of July 1944. The concessions made by Roosevelt were generous to the point of changing the nature of the original plan. Yet Wall Street effectively withheld its support of the Bank and the Fund until 1947.

Among the original proposals [12] withdrawn before the Bretton Woods conference:

- the creation of a currency specific to the Bank. As we have seen, Harry White proposed calling it the *unitas*. John Maynard Keynes had meantime made a similar proposal, the *Bancor,* which was no more successful.
- the Bank's use of own capital when making loans. It was finally decided that the Bank would borrow the capital it needed to make loans from the private banking sector.
- the stabilization of commodity prices.

The two most influential countries in discussions with the U.S. about the adoption of a final proposal were Great Britain and the USSR. Great Britain demanded privileged terms from Washington. For Churchill, any negotiations between Washington and London must be bilateral and secret [13]. Washington preferred to negotiate with all the Allies separately, on the divide and rule principle.

It seems that Franklin Roosevelt, seconded by Harry White and Henry Morgenthau (Secretary of the Treasury), genuinely wished to guarantee Soviet Russia's participation in the establishment of the Bank and the Fund. In January 1944 Henry Morgenthau publicly disclosed that two Soviet delegates had arrived in Washington to discuss the creation of these two institutions.

The geo-political and geo-strategic dimension

Between July 1 and 22, 1944, the United Nations Monetary and Financial Conference, better known as the Bretton Woods [14] Conference, was attended by representatives from 44 countries.

The United States delegation was headed by Henry Morgenthau and Harry White, the British delegation by Lord John Maynard Keynes. These two delegations directed the work of the Conference.

The Soviets were also in attendance. As a result of bargaining between Washington, Moscow and London, the USSR was to obtain third place in terms of voting rights, whereas it had wanted second place. Finally, Moscow did not ratify the final agreements and in 1947, at the UN General Assembly, denounced the Bretton Woods institutions as "*branches of Wall Street*". For the Soviet representative, the World Bank was "*subordinated to political purposes which make it the instrument of one great power*" [15].

The distribution of votes clearly reflected US and British dominance over the two institutions. In 1947, these two countries together had almost 50% of the votes (34.23% for the United States and 14.17% for the United Kingdom on 30 August 1947).

In 1947, the distribution of votes by major categories of countries and regions paints a telling picture of the balance of power in the allied camp (not counting the USSR) immediately after the War. Eleven most industrialized countries held more than 70% of votes [16]. All the countries of the African continent together held no more than 2.34%. Only three African countries had voting rights because practically all the others were still under colonial rule [17]. These three countries were: Egypt (0.70% of votes); the Union of South Africa (1.34%) governed by a white racist power that would introduce apartheid a year later, and Ethiopia (0.30%). In a word, black Africa under a black government (the Emperor Haile Selassie) held just one third of one per cent of the votes.

South and East Asia continent held 11.66%. Only three countries were members: Chiang Kai-shek's nationalist China (6.68%) - a U.S. ally; the Philippines (0.43%) - a U.S. colony until 1946; India (4.55%) - which gained independence from the British crown in 1947.

Central and Eastern Europe held 3.90% (Poland and Czechoslovakia each held 1.60% and Tito's Yugoslavia 0.70%).

The Near East and Middle East had 2.24% (Turkey, 0.73%; Lebanon, 0.32%; Iran, 0.52%; Syria, 0.34%; Iraq, 0.33%).

The whole of Latin America and the Caribbean, a region considered to be firmly allied to the United States, held 8.38% votes spread over eighteen countries: Bolivia (0.34%), Brazil (1.39%), Chile (0.64%), Colombia (0.64%), Costa Rica (0.29%), Cuba (0.64%), Dominican Republic (0.29%), Ecuador (0.30%), El Salvador (0.28%), Guatemala (0.29%), Honduras (0.28%), Mexico (0.96%), Nicaragua (0.28%), Panama (0.27%), Paraguay (0.8%), Peru (0,45%), Uruguay (0.38%), Venezuela (0.38%).

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P.S.

* Paru dans l'Hebdo L'Anticapitaliste - 253 (31/07/2014). http://www.npa2009.org/

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http://cadtm.org/Banks-Fudged-health-report

Footnotes

[1] Bretton Woods is located in the mountains of New Hampshire.

[2] This text has been first edited in French in Eric Toussaint, *Banque Mondiale: Le Coup d'État permanent*, CADTM-Syllepse-Cetim, Liège-Paris-Genève, 2006, chapter one. The book has been edited in English, *The World Bank : A critical Primer*. Pluto Press, 2007.

[3] This section is largely based on: 1) Oliver, Robert W. 1975. International Economic Co-operation and the World Bank, MacMillan Press, London, 421 p; 2) Mason Edward S. and Asher, Robert E. 1973. The World Bank since Bretton Woods, The Brookings Institution, Washington, D.C., chapter 1, p. 11-35; 3) Kapur, Devesh, Lewis, John P., Webb, Richard. 1997. The World Bank, Its First Half Century, Volume 1: History, Brookings Institution Press, Washington, D.C., specifically chapter 2, p. 57-84; 4) George, Susan and Sabelli, Fabrizio. 1994. Crédits sans Frontières, col. Essais, La Découverte, Paris, chapter 1, p. 28-45 ; 5) Rich, Bruce. 1994. Mortgaging the Earth, Earthscan, London, chapter 3, p. 49-80 ; 6) Aglietta, Michel, and MOATTI, Sandra. 2000. Le FMI. De l'ordre monétaire aux désordres financiers, Ed. Economica, Paris, chapter 1, p. 8-31 ; 7) Catherine Gwin, "U.S. relations with the World Bank, 1945-1992", in Kapur, Devesh, Lewis, John P., Webb, Richard. 1997. The World Bank, Its First Half Century, Volume 2, p. 195-200.

[4] Toussaint Eric. 2004. La Finance contre les peuples, chap. 7, p. 173-184.

[5] Oliver Robert W. 1975. p. 72-75, p. 109.

[6] John Maynard KEYNES, Collected Writings, Vol XXI, Macmillan, London, quoted by Payer, Cheryl, 1991, p.20.

[7] The U.S. Department of State is the department responsible for administering the country's foreign policy.

[8] The Chilean representative of the Inter-American Bank, Carlos Davila, wrote on 8 January 1940 : "*In 1938, Germany absorbed 2 percent of the cacao exported by our countries; 25 percent of the cattle hides; 16 percent of the coffee; 19 percent of the corn; 29 percent of the cotton; 6*

percent of the wheat; and 23 percent of the wool. (...) A new and closer form of association will be necessary in order to develop and exploit the mineral and agricultural resources of Latin America with a view to supplying and increasing the products saleable in the United States without domestic competition. A financial, technical and commercial collaboration which can be extended to the industrial field also, and which would permit creating or augmenting the production in Latin America of that large variety of manufactured articles which the United States now cannot or does not wish to import from other continents.

It is advisable from every point of view that the necessary capital to carry out this program come from the United States and Latin America investors. Only thus would a page be turned over the history of the difficulties which United States investments by themselves have encountered." Quoted by Oliver Robert W, 1975, p. 95

[9] Quoted by Oliver, Robert W, 1975, p. 96-97.

[10] Toussaint Eric. 2005. Your Money or Your Life. The Tiranny of Global Finance, Haymarket Books, Chicago, chapter 7.

[11] Quoted by Oliver Robert W, 1975, p. 111-112.

[12] For a full list of the proposals put forward by Harry White and that were abandoned or seriously amended, see Oliver Robert W, 1975, p. 157-159.

[13] Winston Churchill was uneasy about the United States' intentions. He told President Roosevelt: "I believe you want to abolish the British Empire. [...] Everything you say is confirmation of this fact. Yet we know that you are our only hope. And you know we know it. Without America, the British Empire will perish." Quoted by George, Susan and Sabelli, Fabrizio. 1994. Crédits sans Frontières, p. 31.

[14] Bretton Woods is located in the mountains of New Hampshire. The international conference lasted three weeks.

[15] Mason Edward S. and Asher, Robert E. 1973. The World Bank since Bretton Woods, p. 29.

[16] At 30 August 1947: Australia (2.41%), Belgium (2.67%), Canada (3.74%), Denmark (0.99%), France (5.88%), Greece (0.53%), Luxembourg (0.37%), Netherlands (3.21%), Norway (0.80%), United Kingdom (14.17%), United States (34.23%).

[17] Millet Damien. 2005. L'Afrique sans dette, chapter 1.