Keynes Redux: From World Money to International Money at last?

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Abstract

In this article, I argue that Keynes relevance in the current crisis goes deeper than these extensive but superficial references to him reveal. Like several others e.g. Susan George (2007), George Monbiot (2003) and Joseph Stiglitz (2006) I take Keynes *original* proposals at the Bretton Woods conference of 1944 as the starting point for reconstructing world economic and monetary governance for a post-neoliberal world. Unlike them, however, I explain Keynes defeat at Bretton Woods, historically and argue that prospects for an acceptance of his ideas are better today. Unlike them, I also attempt to restore to Keynes ideas their original coherence and integrity. This is necessary because the real inspiration behind Keynes original Bretton Woods proposals is only dimly understood; because these proposals are not easily separated from his ideas about the management of domestic economies for full employment; because, taken together, these ideas constitute a far more radical critique of capitalism than is usually appreciated; because, and partly as a consequence, important disputes over the interpretation of Keynes own ideas, especially between his influential followers who sought to assimilate him into the neoclassical economics he criticised and the small band of those who sought to rescue him from this fate, persist; because the left, for the most part, has tended to see Keynes as a mere reformist and thus not worthy of attention; and because the reasons why so many of the key elements of Keynes proposals were rejected at Bretton Woods remain unclear.

But, perhaps most importantly, Keynes ideas need to be restored to their historical context to uncover the anachronisms that ensured the rejection of his ideas then and which make him especially relevant today. Whereas in 1944 one critical historical condition an international order without a single overwhelmingly dominant economy able to impose its will on all the others for the acceptance of his proposals was still lacking, it is now present. If in 1944 Keynes was tragically ahead of his time, he was *our* contemporary then and it is time to make him so now. This requires a recovery of our historical moment too.

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> I sympathise, therefore, with those who would minimise, rather than with those who would maximise, economic entanglement between nations. Ideas, knowledge, art, hospitality, travel - these are the things which should of their nature be international. But let goods be homespun whenever it is reasonably and conveniently possible; and, above all, let finance be primarily national.
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> - J. M. Keynes, 'National Self-Sufficiency' (1933)

As the first capitalist crisis of the 21st century overturned accepted wisdom of three neoliberal decades, yesterday's convinced neoliberals turned, uncertainly and not ungrudgingly, to their former nemesis, John Maynard Keynes to revive flagging economies. Of course, it was mostly a reflex action; of course, the Keynes they found ready to hand was a popularised and distorted Keynes; and, of course, fragments of neoliberalism still obstructed their vision of even this Keynes.

Internationally, the crisis also put a question mark over the world's monetary arrangements in force since 1971 when the US ended the post-war Bretton Woods system by removing its keystone, the dollar's peg to gold. Bretton Woods, widely credited with the legendary 'Golden Age' of growth, was regarded as Keynesian. The ad hoc arrangements that replaced them – the unilateral imposition of the US dollar, delinked from gold, as the world's *de facto* currency – have been celebrated by some as 'Bretton Woods II' and condemned by others for giving unearned seigniorage privileges to the United States and imposing an iniquitous, unsustainable and deflationary monetary regime on the rest of the world (e.g. Gowan 1999). As the crisis put the longevity of the US dollar as the world's currency into doubt, however, neoliberals could not permit themselves even a grudging and reluctant resort to Keynes, so intimate was the connection between the 'globalized' and financialized world economy which neoliberalism had created and the supremacy of the dollar within it. They probably harbour vain hopes that the US-led financialized world economy might be restored. Nevertheless, calls for a new 'Bretton Woods' also invoked Keynes. Of course, here too, there was the simple resort to what had been accepted wisdom before neoliberalism; here too, it was rarely recalled that the Bretton Woods conference was the site of Keynes' *defeat* on key points of his original proposals; and here too, there was confusion about how exactly Keynes would have differed from 'Bretton Woods II', let alone, the original Bretton Woods.

In this article, I argue that Keynes' relevance in the current crisis goes deeper than these extensive but superficial references to him reveal. Like several others – e.g. Susan George (2007), George Monbiot (2003) and Joseph Stiglitz (2006) – I take Keynes' *original* proposals at the Bretton Woods conference of 1944 as the starting point for reconstructing world economic and monetary governance for a post-neoliberal world. Unlike them, however, I explain Keynes' defeat at Bretton Woods, historically and argue that prospects for an acceptance of his ideas are better today. Unlike them, I also attempt to restore to Keynes ideas their original coherence and integrity. This is necessary because the real inspiration behind Keynes original Bretton Woods proposals is only dimly understood; because these proposals are not easily separated from his ideas about the management of domestic economies for full employment; because, taken together, these ideas constitute a far more radical critique of capitalism than is usually appreciated; because, and partly as a consequence, important disputes over the interpretation of Keynes' own ideas, especially between his influential 'followers' who sought to assimilate him into the neoclassical economics he criticised and the small band of those who sought to rescue him from this fate, persist; because the left, for the most part, has tended to see Keynes as a 'mere reformist' and thus not worthy of attention; and because the reasons why so many of the key elements of Keynes' proposals were rejected at Bretton Woods remain unclear.

But, perhaps most importantly, Keynes' ideas need to be restored to their historical context to uncover the anachronisms that ensured the rejection of his ideas then and which make him especially relevant today. Whereas in 1944 one critical historical condition – an international order without a single overwhelmingly dominant economy able to impose its will on all the others – for the acceptance of his proposals was still lacking, it is now present. If in 1944 Keynes was tragically ahead of his time, he was *our* contemporary then and it is time to make him so now. This requires a recovery of our historical moment too.

The Crisis of the World's Money

For a time the financial crisis seemed to increase the value of the US dollar. Lack of any other reliable reserve asset save gold drove the 'flight to safety' into US treasuries, sending their interest rates into negative territory. This was compounded as nervous US investors repatriated their investments from 'emerging economies' and businesses hoarded cash. But underlying dollar rally, the rest of the world's willingness to hold dollars, effectively to lend the US money, was radically weakening. Since 1971, the world was persuaded to hold dollars through a variety of means including the denomination of the world's oil trade in US dollars, high interest rates, a stock market bubble, the emerging economies' post-1998 compulsion to accumulate high reserves and, most recently, the US housing bubble. The 2008 crisis marked the end of US-led 'financialization' whereby such strategies prolonged US dominance largely by propping up the US dollar and the US-dominanted world financial system.

Financialization had postponed, and even exacerbated, underlying economic weaknesses. When they originally gave rise to the 'declinism' of the 1970s they included rising balance of payments deficits, declining competitiveness, a declining dollar and the threats of continuing gold outflows that had prompted the US to 'close the gold window'. To these, later decades added widening trade deficits and a financialized economy reliant on low wages and high income differentials.

The fate of the latest financial strategy had come to rely on precisely the weak US economy financialization has for decades attempted to evade. The US acted as the 'market of last resort' for market-hungry emerging economies in a deflationary world where demand grew too slowly. The US consumed beyond its means and the rest of the world lent it the money to do so. However, increasing consumption amid stagnant and even declining wages, relied critically on a financial structure which encouraged the substitution of debt for wages. It was never 'easy credit' but given on ever harsher terms to those less and less able to repay.

That structure finally reached the limit of American earners to support and triggered the 'sub-prime' crisis of 2008 and the wider financial crisis followed when its effects reached the larger financial institutions.

The widespread impression that the financial crisis caused the recession is thus mistaken. The US consumer's incapacity to consume – thanks to stagnant wages themselves the result of a stagnant economy whose financialised guise covered up and exacerbated, rather than overcame, its weaknesses – was not the consequence of the crisis, *it was its cause*. While the economies of the rest of the world, especially the fast-growing 'emerging economies' may not have 'decoupled' from that of the US, while they too were in for considerable economic pain, the recession's disproportionate impact on the US could not long remain hidden. Financialization had substituted for real growth there to the greatest extent (only the UK may have surpassed the US on this score), and served to extend a volatile dominance over the world economy. The crisis was the comeuppance of this strategy. (Desai 2007, 2008)

George Soros had already predicted in January 2008 that with 'a recession in the developed world … now more or less inevitable [and] China, India and some of the oil-producing countries ... in a very strong countertrend. ...the current financial crisis is less likely to cause a global recession than a radical realignment of the global economy, with a relative decline of the US and the rise of China and other countries in the developing world' (Soros 2008). The dollar rally was short-lived and the dollar began its steadier slide by the close of 2008. G-20 leaders gathered at Washington DC in mid-November 2008 had already pledged themselves to reform international financial institutions 'so that they can more adequately reflect changing economic weights in the world economy in order to increase their legitimacy and effectiveness.'(Office of the Press Secretary, 2008) Meanwhile, the President of the United Nations General Assembly appointed a Commission of Experts on Reform of the International Monetary and Financial System, headed by Joseph Stiglitz. In what way might Keynes be relevant to these efforts?

Reading Keynes Historically

Keynes, like Marx, mounted a historically informed critique of classical political economy and, in Keynes's case, also the neoclassical economics which emerged in the 1870s to displace it (Dostaler 2007) [1] Unlike Marx, however, Keynes developed his critique through interventions in policy debates from within, rather than outside, the economic and political establishment of his country, a mark of the historically low point to which capitalism had sunk during the Great Depression and the Age of Catastrophe (1914-45) more generally (Hobsbawm 1994). As with Marx, misinterpretations of Keynes abound: Paul Samuelson, most flagrantly perhaps, popularized Keynes as a neoclassical economist. As those who were only yesterday busy burying Keynes come to praise him, in their turn, they erect before us a Keynes to justify bailouts of bankers he would have opposed.

A very different Keynes emerges when we read his work in its historical context, that of the national and international policy battles he fought (Dostaler 2007), and of the traditions

[1] A good part of the difficulties in interpreting Keynes emerge from attempting to read interventions in policy debates written by a thinker deeply aware of the specificity of those historical moments, as if they were works of theory. The underlying unity of thinking was moral and political, not 'theoretical'. I owe much of the deeper understanding I have on this point also to conversations with Victoria Chick.

and questions that inspired his wider – social and moral, and not just economic – thought within the English social liberal tendency that shaded into social democracy and counted among its adherents J.A. Hobson, the Fabians, and Shaw (Clarke 1978). This Keynes is close to that of the left-wing Keyesians and the Post-Keynesians (Chick 1983; Davidson 1991, Tily, 2007) though perhaps even they don't quite reckon fully with the tendency of Keynes' critique of the irrationality and injustices of capitalism to escape the decent liberalism of his own stated convictions[2] into far more radical directions. Keynes claimed to be saving capitalism from itself but it could be doubted whether it remained capitalism after he was done saving it.

This Keynes is also among the few economic thinkers who were not equilibrium theorists, but temporalists (Freeman 2007). Like Marx or Sismondi, he saw economic processes in real time where outcomes were uncertain and expectations could fail to be realised. Actions could not, therefore, be accounted for by rational calculation alone: they were also influenced by uncertainty and fear of the future. Money was critical: '*the importance of money essentially flows from its being a link between the present and the future'* (Keynes 1965: 293). Non-temporal or 'stationary equilibrium' classical and neo-classical theorists relied on the notion of a 'real-exchange economy' in which money is merely a 'neutral link between transactions in real things and real assets'. By contrast, Keynes conceived of a monetary economy as one in which 'money plays a part of its own and affects motives and decisions'(Keynes 1971: XIII: 408-9).

Finally, and most importantly for our purposes, Keynes's critique of the laissez-faire and free-trade views of classical political economy and neo-classical economics – one may call them cosmopolitan – conceived of the capitalist world as fundamentally one of *national* economies requiring *inter-national* economic governance. By contrast, liberals and Marxists alike give nation-states short shrift, the rhetorics of 'globalization' and 'empire' being only their latest pretexts (Desai, 2008). Their image of the capitalist world relies on a 19th century vision of a seamless *economic* world of capitalism in which nations play little or no role. That 19th century idea was, however, little more than the reflection of the imperial 'expansion of England' under the ideology (never the reality) of free trade (Gallagher and Robinson 1953).

Such a cosmopolitan view was never accepted, e.g., by Adam Smith (see Arrighi 2007; Desai, 2009) and, in the 19th century, it was frontally challenged by economic nationalist thinkers such as the German Friedrich List, the Americans Alexander Hamilton and, Henry Carey whose prescriptions powered the economic rise of the principal states – the United States, Germany and Japan – to challenge British industrial supremacy in the late 19th century, and later inspired anti-colonial and nationalist thinkers. Free markets concentrated and reinforced economic advantage though a division of labour in which some nations produced higher value goods – usually industrial – than others. The pattern of economic advantage could only be challenged politically by national development policies. Free-trade thinking, an artefact of Britain's industrial supremacy, was challenged in that country too by the latter 19th and early 20th centuries (Semmel 1960). Relative industrial decline reduced Britain to being one, declining, national economy among others, though she retained the world's largest empire to cushion the worst effects.[3] By the early 20th century Bolshevik ideas

[2] Dostaler 2007 records both his 'allergy' to Marx and his acknowledgement of Marx's insights on critical points, including monetary theory.

[3] There is an extensive literature on British relative decline. See Hobsbawm 1968, Gamble 1994, Leys 1989, Anderson 1992. This literature peaked in the 1980s when some thought the problems had been replaced by

about uneven and combined development touched on these realities but remained too focused on the potential for socialist revolution to really theorise their role in capitalist development except in isolated cases (Löwy 1981; Nairn 1981; Teschke 2003). More recently, Erik Reinert traced this lineage, dubbed The Other Cannon, (REF?) to the beginnings of political economy and its continuing relevance to understanding the patterns of 20th century capitalism underlined by the 'developmental state' literature (Haggard 1990; Deyo 1987; Woo-Cumings 1999; Amsden 2001).

Domestically, popular political energies were increasingly directed towards the nation- state, a process which climaxed in 1914 when the working class parties of Europe forsook internationalism in favour of nationalism and war, shattering the Second International. Shocking though this seemed at the time, the practice of the parties of the Second International had for decades been reformist and national even as rhetoric remained stridently revolutionary and internationalist (Joll 1974; Schorske 1983). 1914 merely demonstrated that nation-states were the principal site for what Karl Polanyi called the 'double movement'(Polanyi 1957)—the answering movement of social protection to counteract the corrosive effects of the market on society.

Keynes' critique of classical political economy and neo-classical economics pivoted on this national and international world. It also contributed to and reinforced it. Pioneering national economic aggregates, he transformed the discipline, giving it a new branch: macroeconomics. He also he initiated national income accounting which was adopted internationally after the war through the United Nations System of National Accounts. It is so intrinsic to economic policy making and debate that we forget that 'Until well into the depression the United States had no useful figures on the level or distribution of employment. There was a certain classical logic to this; one did not spend money collecting information on what, in high economic principle, could not exist'. National income

> showed the value of the total production of goods and services of all kinds, public and private. The Gross National Product. And in companion tables, they showed the income derived therefrom by kind and source. National income. That the latter needed to be sufficient to buy the former was a thought that no one could henceforth escape. Nor, more specifically, the thought that savings from the income now shown might not all be used – that they might not be absorbed by the spending for investment goods also shown in the tables. And it was evident how serviceably an increment of income, as from government expenditure, would make up any shortfall investment spending or consumer borrowing and add to the purchase and production of goods. (Galbraith 1971: 245-6)

Three decades of neoliberalism were unable to dislodge the assumptions and practices that lay behind such national economic management. The associated welfare state, which also proved very hard to dislodge (Esping-Anderson 2002), put a floor below demand in western societies and it is likely to account for the biggest differences between the present crisis and the Great Depression. For all their strident commitment to *laissez faire,* neoliberals operated within, this Keynesian framework of national economic management. Of course, they pursued different purposes, and even used different means: e.g stimulating demand through Reganite military spending or, ironically, through Greenspanite credit expansion.

'globalization' but they are resurfacing, if newspaper comment is anything to go by. See also the excellent analysis of the persistence of the problems, globalization notwithstanding, in Coates 2005.

The Radical Keynes

Keynes's critique of the classical and neo-classical traditions was thoroughgoing. Where they took the level of economic activity and employment as a given, he took it as his chief explanandum. Where they assumed away the problem of unemployment, he emphasised its reality. Where they thought saving virtuous, to be rewarded by interest, he criticised it as a vice of the 'functionless investor', to be discouraged by reducing interest close to zero to 'euthanise the rentier'. Where they loathed and feared state intervention, he advocated its use, up to and including the 'socialisation of investment' to achieve full employment. Where they opposed protectionism, he advocated a national economy. And where it worshipped at the altar of the gold standard, Keynes exposed its contingent operation and its politically managed reality. The classical and neo-classical traditions implicitly assumed a self-equilibrating market, accepting Say's law that supply created its own demand and 'would collapse without it' (Keynes 1965: 19). They also assumed that money made no difference so that savings axiomatically equalled investment and crises were inconceivable. At best, they constituted 'a theory of distribution under conditions of full employment' (Keynes 1965: 16).

Keynes regarded unemployment, never very low in the inter-war years, as the main problem of capitalism and sought to show that it could be solved within capitalism. He sought to produce a theory of the aggregate level of production, and therefore employment, in a monetary economy where 'changing views about the future are capable of influencing the quantity of employment'.(Keynes 1965: xxii). What levels of effective demand (demand at prevailing prices) for consumption and investment were required to keep economies operating at full employment, i.e. 'a situation in which aggregate employment is inelastic in response to an increase in effective demand for its output' or where available labour was employed and additional increases in effective demand would not increase the level of employment.(Keynes 1965: 26). The translation of incomes into effective demand depended on their level, their distribution, the proportion spent on consumption (the propensity to consume) and the 'liquidity preference' of savers, i.e. their willingness to part with their command over future resources for specified amounts of time, rather than keeping them liquid.

In addition to high wages, high employment levels and egalitarian income distribution, adequate levels of employment depended on whether savings were invested in further economic activity, or kept liquid in financial investment characteristic of rentiers. If this happened, the state would need to step in. The scale of state intervention Keynes envisages is often not widely appreciated:

> The State will have to exercise a guiding influence on the propensity to consume partly through its scheme of taxation, partly by fixing the rate of interest, and partly, perhaps, in other ways. Furthermore, it seems unlikely that the influence of banking policy on the rate of interest will be sufficient by itself to determine an optimum rate of investment. I conceive, therefore, that a somewhat comprehensive socialisation of investment will prove the only means of securing an approximation to full employment; though this need not exclude all manner of compromises and of devices by which public authority will co-operate with private initiative.'

While this was not state socialism nor state ownership of the means of production, nor was it capitalism in any clearly recognizable form. Not only did Keynes envisage 'a large extension in the traditional function of government' (Keynes 1965: 379), narrowing the role of capitalist entrepreneurs, they were no different from labour. Entrepreneurship consisted of 'the personal services of the entrepreneur and his assistants' (Keynes 1965: 213-4). These played a useful role, 'forecasting the prospective yield of assets over their whole life', and were to be sharply distinguished from rentiers, the 'functionless investor, merely 'forecasting the psychology of the market' (Keynes 1965: 158; Chernomas 1984; Dillard 1948).

Rentiers stood between society and 'that degree of material well-being to which our technical advancement entitles us'. Interest was supposed to be an inducement to save but, Keynes showed, excessive saving could hinder growth and that 'the extent of effective saving is necessarily determined by the scale of investment and that the scale of investment is promoted by a *low* rate of interest'(Keynes 1965: 375). Thus, 'We might aim in practice ... at an increase in the volume of capital until it ceases to be scarce and the functionless investor will no longer receive a bonus' (Keynes 1965: 376)

> this state of affairs would be quite compatible with some measure of individualism, yet it would mean the euthanasia of the rentier, and, consequently, the euthanasia of the cumulative oppressive power of the capitalist to exploit the scarcity value of capital. Interest to-day rewards no genuine sacrifice, any more than does the rent of land....
>
> in the event of the individual propensity to consume proving to be of such a character that new saving in conditions of full employment comes to an end before capital has become sufficiently abundant ... it will still be possible for communal saving through the agency of the state to be maintained at a level which will allow the growth of capital up to the point where it ceases to be scarce. (Keynes 1965: 375-6).

Internationally, Keynes' inveighed against Ricardian notions of free trade and for 'a greater measure of national self-sufficiency and economic isolation between countries than existed in 1914'. The Great War showed that such a policy was most likely to 'serve the cause of peace, rather than otherwise. At any rate the age of economic internationalism was not particularly successful in avoiding war'. (Keynes 1933) He clearly saw the link between 'free trade' and imperialism:

> The protection of a country's existing foreign interests, the capture of new markets, the progress of economic imperialism - these are a scarcely avoidable part of a scheme of things which aims at the maximum of international specialisation and at the maximum geographical diffusion of capital wherever its seat of ownership.

It was necessary to 'gradually bring ... the producer and the consumer within the ambit of the same national, economic and financial organisation'.

> Experience accumulates to prove that most modern mass-production processes can be performed in most countries and climates with almost equal efficiency. Moreover, as wealth increases, both primary and manufactured products play a smaller relative part in the national economy compared with houses, personal services and local amenities which are not the subject of international exchange; with the result that a moderate increase in the real cost of the former consequent on greater national self-sufficiency may cease to be of serious consequence when weighed in the balance against advantages of a different kind. National self-sufficiency, in short, though it costs

> something, may be becoming a luxury which we can afford if we happen to want it. (Keynes 1933)

Keynes also opposed ' a system by which the rate of interest finds, under the operation of normal financial forces, a uniform level throughout the world, after allowing for risk and the like' – because it would be militate against the reduction in the interest rate, and the euthanasia of the rentier, necessary to red capitalism of its more oppressive features. (Keynes 1933).

Keynes' Original Proposals

What structures of world economic governance were most likely to enable these national economic policies? Keynes' thinking on this was already present in *Indian Currency and Finance* (1913) – the rational management of money to sub-serve adequate levels of activity in the real economy. It developed further through his critique of the pre-1914 gold standard and interwar efforts to reconstitute it which echo into our time.[4] Like Marx (Freeman 2004), and Simmel (2004), Keynes saw money as a product of state and society, not a natural creation(See also Ingham 2004).

Keynes objected to gold, or any 'freely convertible international standard' because the idea of their automatic functioning – i.e. the idea that trade deficits would automatically be solved by outflows of gold from the deficit country, bringing down its exchange rate and prices and/or stimulating exports – relied on the discredited quantity theory of money. Such arrangements were typically deflationary, throwing 'the main burden of adjustment to trade and payments imbalances on the country which is in the *debtor* position on the international balance of payments, - that is on the country which is (in this context) by hypothesis the *weaker* and above all the *smaller* in comparison with the other side of the scales which (for this purpose) is the rest of the world' (Keynes 1980: 27). Moreover, adjustment was '*compulsory* for the debtor and *voluntary* for the creditor'. And, in so far as adjustment operated through exchange rates, it would only stimulate exports 'by reducing their international price in terms of imports' (Keynes 1980: 29) imposing social and economic disruption of an unwarranted severity on already weak economies.

Systemically, a gold standard left the expansion of liquidity to be determined by the vagaries of gold discovery and production and not the pace of growth of trade. It had only *seemed* to work briefly in the 19th century because discoveries of new deposits had, exceptionally in the short history of gold as money, kept pace with the expansion of production ('Auri Sacra Fames' Keynes 1963; Vilar 1991) while in the age of Elizabeth, the only other time a metallic standard seemed to world automatically, 'the prodigious augmentation of the supply for silver from the new world was substituting the features of inflation for those of deflation (bringing a different sort of evil with it)' (Keynes 1980: 30)

Two other objections to the gold standard are relevant today. First, with economic and financial dominance having passed on to the US, Keynes saw clearly that adopting the gold standard would subject Britain's economic fate to developments and decisions in the US (Dostaler 2007: 211) and make assuring national employment and price levels difficult. Secondly, the free capital movements that went with a gold standard were likely to be a major

[4] FT, 'Gold is the Only Alternative'

problem. While during the 19th century, London's role as a financial centre for overseas investment had translated inflows of gold 'not in the first instance into a change in prices and wages, but into a change in the volume of foreign investment by the creditors' (Keyes 1980: 30) (incidentally also transferring the '*onus* of adjustment from the debtor to the creditor position'(Keynes 1980: 21), in the interwar period, the combined problems of the structure of inter-allied debts, which were ultimately owed to the US and were not applied to productive purposes, and of refugee and speculative capital flowing to the US even from trade deficit countries, spelled disaster. 'Nothing is more certain than that the movement of capital funds must be regulated'. (Keynes 1980: 31). While gold remained a major element in world reserves, it could not be the foundation of the monetary order of a world vastly more productive and dynamic than in the 19th century.

Not being a viable basis for the currency of an expanding and dynamic world economy, gold was already a 'barbarous relic' (Keynes 1963: 179; See also Keynes 1999). By the inter-war period it had already

> become a 'managed currency'.... Now that most countries have abandoned the gold standard, the supply of the metal would, if the chief user of it restricted its holdings to its real needs, prove largely redundant. The United States has not been able to let gold fall to its natural value, because it could not face the resulting depreciation of its standard. It has been driven, therefore, to the costly policy of burying in the vaults of Washington what the miners of the Rand have laboriously brought to the surface. Consequently gold now stands at an 'artificial' value, the future course of which almost entirely depends on the policy of the Federal Reserve Board of the United States. (Keynes 1963: 175-6)

In fact, Marcello de Cecco was only extending the logic of Keynes' arguments about the gold standard's unworkability when he showed that it has never worked 'automatically' in a world of nation-states competing to increase growth:

> In none of the cases … did those who implemented monetary reform have the slightest intention of linking their countries to an international monetary system which would then automatically produce a kind of international economic meritocracy, based on differences in prices and interest rates among the various nations. … The various governments adopted such economic policies as they deemed would best serve the interest of the ruling classes. They favoured fixed exchange rates when they were expedient and progressive devaluation when it appeared possible. Nor were they afraid to change course whenever they felt it was necessary. Moreover, uncertain and even downright self-contradictory economic policies were adopted – as they often are nowadays. It would therefore be misleading to postulate any important qualitative differences between the monetary policies of the period under review and those of our own time. (De Cecco 1984: 60-61).

Keynes' first scheme for a replacement for gold as international money appeared in the *Treatise on Money* in 1923 and his original proposals for Bretton Woods, outlined in 1941 and 1942 and adopted as the official position of the British government, were based on the further refinement and elaboration of these ideas. They were, as Geoff Tily pointed out, subject to a 'two-stage dismantling' 'First, at Bretton Woods Keynes' proposals were watered down' through the 'excessively inelastic exchange system not dissimilar to the gold standard', though the final agreements has the 'virtue of preserving capital controls'. 'The second stage was the dismantling of Bretton Woods in the early 1970s and the financial liberalisation effected over the 1970s and the start of the 1980s' (Tily 2007: 8).

Keynes' original proposals were nothing if not ambitious. The breakdown of international trade and payments and the depressed levels of economic activity called for nothing less. They aimed to provide the world with the national and international liquidity required for growth and the levels of trade consonant with it. National authorities were to be free to control domestic productive arrangements, particularly free to pursue full employment and progressive social policies. Three key points of his plan deserve our attention today: financial repression' or capital controls to prevent the build-up of excessive obligations, placing of the burden of adjustment on trade surplus countries as well as deficit countries, and a multilaterally managed world currency (not the currency of any single nation) to settle trade imbalances. These three features were not only the most innovative then, they rejection explains the failure of Bretton Woods and are even more relevant today, especially in light of the problems of both developed and, in particular, developing countries under to so-called 'Bretton Woods II' arrangements.

Restoration of economic activity rested on the autonomy of national economic management and capital controls were key.

> Freedom of capital movements is an essential part of the old *laissez-faire* system and assumes that it is right and desirable to have an equalisation of interest rates in all parts of the world. It assumes, that is to say, that if the rate of interest which promotes full employment in Great Britain is lower than the appropriate rate in Australia, there is no reason why this should not be allowed to lead to a situation in which the whole of British savings are invested in Australia, subject only to different estimation so risk, until the equilibrium rate in Australia has been brought down to the British rate. In my view the whole management of the domestic economy depends on being free to have the appropriate rate of interest without reference to the rates prevailing elsewhere in the world. Capital control is a corollary to this. (Keynes 1980: 149).

Capital controls were embodied in the final Bretton Woods agreements and are credited with creating the conditions for the high rates of growth witnessed in the 1950s and 1960s. They were lifted in one country after another in the 1970s and 1980s. Contrary to neoliberal claims that this would ensure that money would flow from 'capital rich' to 'capital poor' countries, the decades since then have been characterised by South to North flows of capital. Indeed, Bretton Woods II' monetary (dis)order of dear money, free and increasingly speculative capital movements, the accumulation of huge trade and payments imbalances and low growth could have been easily predicted on the basis of Keynes analysis.

Keynes' proposals on trade and payments sought to prevent unsustainable imbalances which could undermine growth by imposing deflation on debtors as part of the 'adjustment' process, not unlike the IMF imposed 'Structural Adjustment' of the 1980s and 1990s. Keynes' solution was brilliantly simple: to make running persistent export surpluses unattractive. He proposed an International Clearing Union (ICU) with its own currency – the 'Bancor' – whose value would be 'fixed (but not unalterably) in terms of gold and accepted as the equivalent of gold' (Keynes 1980: 111). Each country would start with an overdraft facility which was proportional to its trading needs. Bancor would be used to account for transactions between nations and their surpluses and deficits, at a world level, would cancel each other out. Interest would be charged on both credit and debit balances at year-end, a measure to induce countries to balance their trade annually. Deficits would be discouraged by not permitting member states to run debit balances over a specified proportion of its quota (25%) in a year without permission of the Governing Board. When such deficits occurred, adjustments would include some leeway for national economic priorities, *permitting* the country to devalue up to 5%. Larger deficits brought on harsher sanctions: requiring the country to devalue by 5%, control its outward capital movements and surrender a suitable proportion of gold reserves in case of a debit balance exceeding half the quota in a year; and requiring it to undertake measures to rectify its trade structure and declaring it in default in case of greater and more persistent debit balances.

However, the ICU plan recognised that deficits of some countries were the other side of the coin of surpluses of other countries and its inducements against running persistent trade surpluses included ensuring that credit balances could not be converted into gold (meaning that creditor countries could only accumulate bancor balances) and charging interest on these credit balances (Keynes 1980: 118-9). In addition, the proposals provided that:

> A member state whose credit balance has exceeded a *half* of its quota on the average of at least a year shall discuss with the Governing Board (but shall retain the ultimate decision in its own hands) what measures would be appropriate to restore the equilibrium of its international balances including –
>
> a) Measures for the expansion of domestic credit and domestic demand;
>
> b) The appreciation of its local currency in terms of bancor, or, alternatively, an increase in money wages'
>
> c) The reduction of excessive tariffs and other discouragements against imports;
>
> d) International loans for the development of backward countries. (Keynes 1980: 120).

Finally, being the currency of no particular country, Bancor would give no country seigniorage privileges. Nor would it leave the world's money hostage to the domestic priorities of any single country nor yet impose on that country the peculiar obligations emerging from issuing the world's means of payment. Keynes' explicitly allayed American fears on this score even as he sidestepped their efforts to disguise their pursuit of self interest as largesse:

> There is no foundation whatever for the idea that the object of the proposals is to make the United States the milch cow of the world in general and of this country in particular. In fact the best hope for the lasting success of the plan is the precise contrary. The plan does not require the United States, or any other country, to put up a single dollar which they themselves choose to employ in any other way whatever. The essence of this is that if a country has a balance in its favour which it does not choose to use in buying goods or services or making overseas investment, this balance shall remain available to the Union – not permanently, but for just to long as the country owning it chooses to leave it unemployed. (Keynes 1980: 276).

Sterling had been able to perform this role relatively well due to a peculiar historically evolved structure of British capital, particularly the place of financial capital within it (Ingham 1984), and even this structure needed the backing of an empire and fortuitous historical circumstances. The geopolitical and geoeconomic configuration of the age national economic management (and international economic competition for catch-up), had already rendered the gold-sterling standard unviable. The largely inward-looking continent-sized US economy, despite its impressive relative size, could not play this sort of role. The added weight of new entrants in this game thanks to decolonization, the needs for both post-war reconstruction and development, meant that the international currency could no longer be the currency of an individual country.

Schumpeter once wrote that 'Keynes's advice was in the first instance always English advice, born of English problems'(quoted in Skidelsky 2000: 293) and it may be objected that Keynes was fighting for Britain's interests alone. However, in speaking for a country in both a trade and financial deficit position (about to get worse due to the impending decolonization), he spoke in an interest more general than the spokesman for the US, the world's greatest economy accounting for 40% of its manufacturing and more than half its GDP , and the world greatest creditor, accounting for 70% of the world's gold reserves thanks to the vast hoard of gold accumulated in the US during the wars and Depression of the previous 3 decades.

The Vanity of US Hegemony

Keynes' original proposals for Bretton Woods rested on Keynes most developed economic understanding, based on decades of critical and iconoclastic work. 'These proposals may have been rejected on political grounds; they were never rejected or disputed on economic grounds.' (Tily 2007: 79). What ensured the rejection of the Keynes plan was precisely configuration of US power.

> The Agreement was shaped not by Keynes' general theory, but by the US desire for an updated gold standard as a means of liberalising trade. If there was an underlying ideology, it was Morgenthau's determination to concentrate financial power in Washington. (Skidelsky 2000: p. 357)

Keynes himself grew bitter towards the end of the negotiations which he has entered into with hope and optimism.

> The Americans at the top seem to have absolutely no conception of international cooperation; since they are the biggest partners they think they have the right to call the tune on practically every point. If they knew the music that would not matter so much; but unfortunately they don't.[5]

The music they did not know was the music of inter-nationalism. The end of the Second World War had found the US the world overwhelmingly dominant economic and financial power, with nearly half the world's manufacturing and more than 70% of its gold reserves. It was not willing to pass up the chance to play the role in the 20th century world economy which the UK had played that of the 19th (Desai 2007; Bacevich 2002; Williams 1972) – exercising hegemony over the world order as its leading industrial and imperial power, providing it with 'public goods' like a world currency (Kindleberger 1975: Arrighi 1994). There seemed no reason it could not: its economic and financial dominance over the rest of the world in the middle of the 20th century seemed even more overwhelming than that

[5] J. M. Keynes, *The Collected Writings of John Maynard Keynes*, London: Macmillan, 1971-89 (30 Vols.), 26, p. 217. Quoted in Gilles Dostaler, *Keynes and His Battles*, Cheltenham: Edward Elgar, 2007, p. 225.

of the UK in the 19th and, though not an extensive colonial power, it exercised an informal imperialism which critical opinion in particular was impressed with.

Precisely the points – an international currency and creditor- and surplus-country obligation share in the burden of adjustment – necessary to govern a Keynesian world of *national* economies were omitted from the final design of Bretton Woods. Worse, in short order the minimally multilateral character, embodied in the IMF, took a back seat to US 'leadership'. US rhetoric after the Second World War overflowed with altruism but US actions were aimed at securing US interests and the continued expansion of the US economy at a pace as to maintain its relative power in the world. Marshall plan aid, usually seen as an act of great enlightenment and altruism, kept the US's extended wartime economy humming and combated Communism in Western Europe. The gold backing provided to the dollar, usually seen to have placed its vast gold reserves at the service of the world, was simply an expedient to put the US's vast reserves of gold, swelled by refugee inflows in the inter-war period, to some use. According to a US senator, it had 'no actual value at all, more than its value for commerce. In putting up a few billions of gold in this great enterprise [the US was] merely attempting to salvage the value of that gold itself' (quoted in Hudson 2003: 150). What is particularly ironic, however, is that the unravelling of US hegemony and the US-dollar centered monetary order were inevitable precisely because in attempting to construct its own imperial order, the US overlooked insistent national and international realities.

To begin with, even more than the UK, the US was and remained a national economy and as such inherently unable to take the deflationary consequences of such responsibilities the way Britain has been able to in the 19th century when popular pressures on national economic policy were lower. By the mid-20th century, the US needed, and by the Keynesian Employment Act of 1948, was required to, to run its economy so as to keep up domestic levels of employment and this frequently ran directly counter to keeping up the value of the dollar (Calleo: 1982). Indeed, the dollar's acceptability as the world's currency ran into trouble as soon as the Bretton Woods agreement came into fuller operation with currency convertibility in 1958. Throughout the 1960s the US's expansionary policies led to inflation and more and more European countries demanded gold in preference to an overvalued dollar. Initially the resulting outflows of gold were stemmed through the creation of a 'gold pool' but the process could only end in the 'closing of the gold window' and the end of Bretton Woods.(Hudson 2003).

Of course, domestic inflation was not the only problem: as a national, rather than a formally imperial or colonial economy, the US faced three further problems. First, whereas Sterling's international acceptability rested to a significant extent on London's role as a financial hub where the empire's trade surpluses were translated into British capital exports, the only way in which the US dollar could be the basis of world liquidity was if the United States ran persistent balance of payments deficits, supplying the world with dollars. As the same time, as Robert Triffin showed, it would only be a matter of time before the world's dollars grew to the point where the gold backing them was insufficient. But, and here was the other horn of the 'Triffin Dilemma' if the deficits ceased, the world would have too little liquidity.

The Triffin Dilemma was compounded by the second problem: the US financed its imperial obligations on the back of a national economy and citizens (as fighting forces), not an empire (with colonial subjects to fight colonial wars), as the UK had done in the 19th century. And in the 1950s and 1960s, while it still ran trade surpluses, its balance of payments was regularly in deficit, demonstrating the inability of its export earnings to finance its imperial obligations, contributed to the dollar's difficulties in the 1960s. For a while these deficits were seen as functional to the system, of course, providing the world with liquidity, and the world even seemed to want more and complaining of a 'dollar shortage' in the 1960. However, by the 1960s the dollar shortage has become a dollar glut as the world had quite enough of inflated dollars.

Finally, lack of a formal empire also meant that unlike the UK, it did not have access to the resources of a formal empire to back up its currency when domestic economic strength failed to do so beginning in the 1970s. The US's loss of competitiveness and resulting trade deficits have made it the world's greatest debtor rather than the world's greatest creditor, as the UK has been in the 19th century and for decades after its relative industrial decline began in the 1870s, up to 1914. While the series of devices which the US resorted to since 1971 to persuade the rest of the world to accept dollars, it was an unsustainable arrangement which has probably seen its end in the present crisis.

On reflection, it is clear that the dominance of the UK in the 19th century and the US at the middle of the 20th century were products exceptional circumstances in the evolution of the international capitalist order. The UK dominated the world economy because it was the first industrial capitalist country in a world of pre-capitalist and pre-industrial producers of agricultural and relatively primitive '*manu*factures' or hand-made products. As we have seen, however, its industrialization gave rise to competing state-sponsored industrialization efforts and as soon as these countries industrialised in the late 19th century, the UK's leading position began to be undermined. If anything, the US's economic and financial dominance was even more exceptional. Its leading position, despite its giant continental size, was due to the great destruction caused by the Second World War in the rest of the capitalist world and the great boost given by it to the US's own economy. The size of the US economy doubled between 1939 and 1945 (and would not double again for the next 22 years, despite the 'golden age' of growth that followed). As soon as Western Europe and Japan recovered from the war's destruction in the late 1960s, the US position was jeopardised. Since then, other countries have begun to industrialise and the possibility that the US or any other country can dominate world economic and financial arrangements now appears closed. International cooperation rather than hegemony is the only way out. Keynes' original proposals remain the best starting point for this.

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