THE DUTCH AND THE AMERICANS IN THE BRETTON WOODS INSTITUTIONS

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Introduction

The Netherlands and the United States both belong to the forty-five founding nations of the International Monetary Fund (IMF) and the World Bank. The Bretton Woods institutions were established at a time when there was consensus among countries about the desired shape of the international monetary system. As an open economy, dependent on international trade, the Netherlands has been interested in arrangements that maintain global economic welfare and foster international trade. Over the years the Netherlands has taken a fairly consistent approach toward the Bretton Woods institutions. Dutch experts helped shape the IMF's approach toward balance-of-payments adjustment. Conversely, the U.S. has changed its attitude over time as it turned from a surplus into a deficit country and did not want to adjust its own domestic policies. Recently, the positions of both countries have become more aligned as the focus has shifted from monetary to financial stability issues under the influence of globalization.

The Negotiations in Bretton Woods

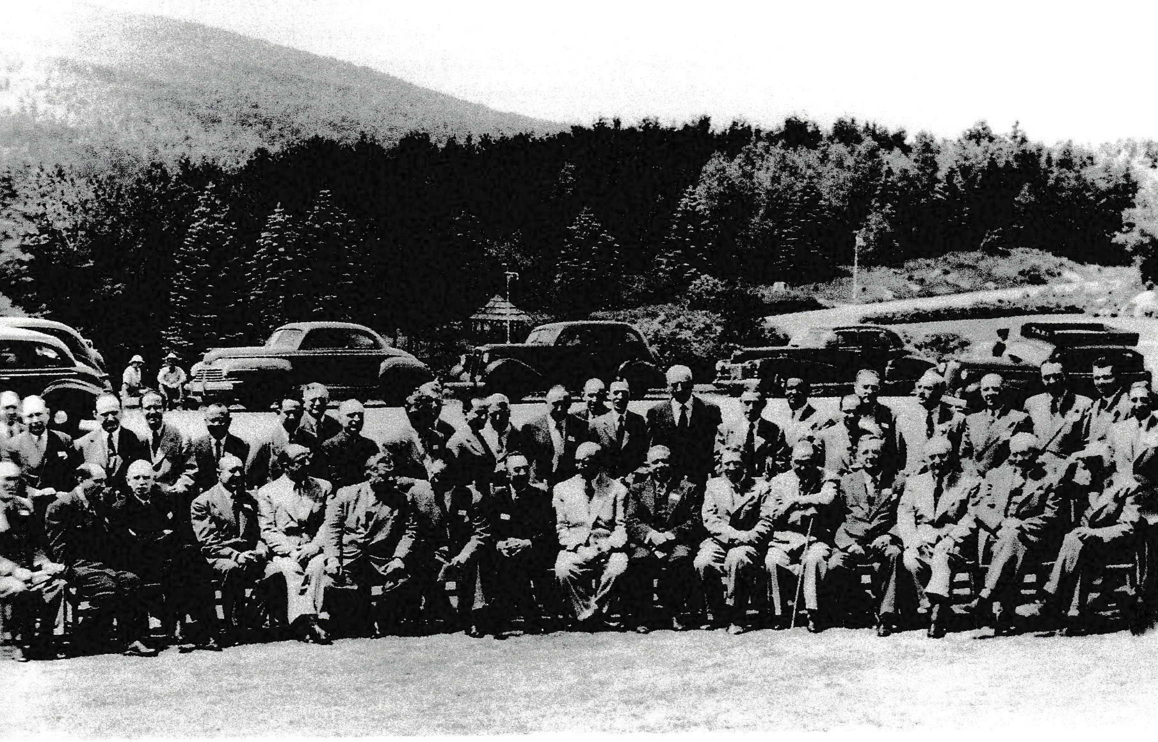
During World War II the United States and the United Kingdom worked out the basic outlines of a postwar monetary system that would avoid the recurrence of competitive devaluations as had occurred during the Great Depression of the 1930s. At the same time, the U.S. was keen to prevent that the rather far-reaching proposals of Keynes, the British spokesman, for international monetary reform might lead to the United States providing practically unlimited financing to the rest of the world.[1]

The cautious U.S. attitude appealed to the Dutch delegation — headed by Johan Willem Beyen, the former president of the Bank for International Settlements — at the 1944 Bretton Woods conference where the outlines of Fund and Bank were agreed upon. Beyen was somewhat skeptical about the proposals and favored regional solutions to monetary problems, as evidenced by his personal involvement with the monetary Benelux agreement of 1943.[2] However, at Bretton Woods radically different proposals were not on the table and Beyen had no way of pushing his own ideas as he had to operate under instructions from The Hague.

The Netherlands delegation realized that the direct advantages that the IMF and World Bank could offer to the open Dutch economy were rather limited, but that their main advantage lay in their mission to improve the global economic situation and foster world trade. The Netherlands had been active in promoting international monetary arrangements in the 1930s and it was no coincidence that it had been the last country to leave the gold standard, in 1936. Therefore, it was attracted to any disciplinary mechanisms that the envisaged monetary system could provide. It shared with the U.S. a firm belief in fixed exchange rates. In the Dutch view, too much flexibility in exchange rate arrangements would provide too much freedom to shift the adjustment burden to other countries. The preference for disciplinary mechanisms that would force countries to adjust, would be a constant theme in the postwar position of the Netherlands.

However, the major theme of the Dutch delegation at Bretton Woods was that Fund and Bank should be established in a financially sound way. For the IMF this implied that the use of its resources should be safeguarded from undue use. In the informal preparatory meetings the Netherlands was among the countries that suggested that greater pressure be exerted by the Fund on debtors and that the use of credit be circumscribed for specific purposes.[3] Whereas other countries were rather lenient as they themselves expected to benefit from Fund drawings, the Netherlands delegation emphasized financial discipline and, therefore, was a natural ally of the Americans in creating safeguards to prevent the usable resources of the IMF — in the initial years mainly consisting of U.S. dollars — from being depleted too quickly.

For the World Bank the Dutch similarly pressured for strict caps on the amounts it could lend, in order to preserve its good standing in global capital markets. The Dutch delegation was composed of experienced practitioners. They were aware of the large losses American institutional investors had incurred on defaults of foreign entity loans in the 1930s. It was clear that the World Bank could only become a success if American investors were absolutely sure of the soundness of the claims on this new institution.



The participants at the international financial conference at Bretton Woods, NH, that took place from July 1 to July 22, 1944.

Unlike other countries, such as France and the Soviet Union, the Dutch did not push to increase their relative share in the institutions. The Netherlands authorities were reluctant to deposit too much of their gold holdings at the IMF, quota payments being made partly in gold. Neither did they want to assume large risks of losses in case the IMF were to be a failure or if guarantees for the World Bank would have to be invoked.

The Early Years

There were relatively few transactions at the Bretton Woods institutions in the initial postwar years as they had to get organized and work out their proceedings. The IMF was primarily involved in establishing the right par values for the exchange rates of its members, which did not come to a resolution until European countries devalued vis-à-vis the U.S. dollar in 1949. In the meantime, the Marshall Plan (1948–51) provided the principal flow of finance to Europe. The U.S. Treasury was unwilling to grant any IMF credit to countries that received Marshall aid.[4] Ironically, the Netherlands, which had been such a staunch supporter of financial discipline at Bretton Woods, was to be the first country to suffer from this attitude.

In May 1947, the Netherlands was the second country after France to use the Fund's resources, albeit for a minimal amount. However, a second request in 1948 got a frosty reception from the U.S. executive director who questioned whether the use of the Fund's resources would be temporary, as the Netherlands had a large budget deficit and was experiencing inflationary pressures. Eventually the loan was approved, but staff were sent to the Netherlands to examine the economic situation.[5] A third request gave rise to the first systematic discussion in the board on the use of IMF resources, in which the U.S. executive director formulated criteria that would assure that credit would be temporary. These criteria foreshadowed the principle of conditionality that has governed IMF credits ever since.[6]

The dissuasive U.S. position was also inspired by increasing doubts about the appropriateness of the exchange rates set after World War II. When the Netherlands in 1949 again applied for a loan, the U.S. director objected and the decision was postponed time and again. Eventually the Dutch request was withdrawn and the guilder was devalued by 30 percent vis-à-vis the U.S. dollar, along with other European currencies. In 1951, another loan to the Netherlands was refused because the financial position was not deemed safe enough.[7] In December 1958 the convertibility of the guilder was restored, along with that of other European currencies. From this time on, the Netherlands took up a creditor position in the IMF.

For postwar reconstruction the Netherlands received a number of loans from the World Bank. These did not meet with the resistance experienced at the IMF. However, an application in 1947 brought with it a barrage of protest letters against granting a loan to a country that did not wish to give independence to its colonies (Indonesia). World Bank President McCloy, an American, withstood this pressure (including a protest letter from his mother) and defended the institution's nonpolitical nature.[8] Moreover, Finance Minister Lieftinck convinced the American bankers that plans to nationalize Dutch enterprises, as advocated by his own Socialist Party, would not materialize. The World Bank loan helped the Netherlands accept a ceasefire in Indonesia and start negotiations under the auspices of the Security Council. Lieftinck later joined the World Bank and IMF executive boards for a prolonged period.

A Dutch Approach in the IMF

Among the members of the original Dutch delegation at Bretton Woods was J. J. Polak, who later became the director of the IMF's Research Department. Polak became one of the intellectual heavyweights in the IMF and his name is associated with the analytical framework for the Fund's financial assistance.[9] He had worked at the League of Nations in Geneva, where together with (future) Nobel laureate Jan Tinbergen he coauthored an econometric macro model of the U.S. economy. Tinbergen had been a major force in the transformation of economics into a model-building discipline and Polak was to build on this experience at the IMF by incorporating a distinctive monetary dimension in the models.

At the same time, the monetary approach to balance-of-payments problems was developed at the Nederlandsche Bank, the Dutch central bank. Governor Holtrop was a proponent of a monetary approach to economic problems in which a clear distinction is made between domestic and foreign sources of liquidity creation.[10] As early as 1950 he observed that balance-of-payments deficits that led to reserve losses always coincided with inflationary domestic financing. In the early 1960s Polak and Holtrop intensively debated the merits of the monetary models used in both institutions. The approach gained recognition when successfully applied in 1969 in an IMF program for the United Kingdom.

From Dollar Shortage to Dollar Glut

The United States for a long time could ignore its own balance-of-payments position because the rest of the world had a thirst for dollars. Around 1960, however, when European economies had recovered significantly and the dollar shortage was long over, observers started to talk of a dollar "glut." European central banks began to worry about the quality of their dollar reserves and converted them into gold. The U.S. reacted, not by adjusting domestic policies, but by organizing bilateral swap arrangements with other central banks, including the Nederlandsche Bank, in order to counter speculative flows that might destabilize major currencies. Eventually, the General Arrangements to Borrow (GAB) were developed to enlarge the potential resources of the IMF, should the U.S. need assistance, and the SDR was promoted as a supplementary reserve currency to the dollar.

The Europeans, however, were not prepared to lend passively to the IMF, which they felt was U.S.-dominated, and insisted on procedures under which they themselves could decide upon a proposal of the IMF managing director. This gave birth to the Group of Ten and a period of intensive transatlantic consultations. Although there was criticism from nonparticipating countries Lieftinck, the Dutch executive director, described the GAB as a "compromise between the ideology of the Fund as a global monetary institution and a newer ideology which sought solutions by closer cooperation between the main industrial countries."[11] From this time there was regular attendance by Federal Reserve officials at the monthly BIS meetings, chaired by Governor Holtrop in his capacity as president of the BIS.

The dialogue between Europe and the United States was diverted from the executive board rooms in Washington to smaller groupings. At the initiative of President Kennedy Working Party 3 was established at the OECD, comprising the Group of Ten countries, and Dutch Treasurer General Emile van Lennep was chosen as its chairman. A major issue was the distribution of the burden of adjustment over deficit and surplus countries. The U.S. had become a deficit country and it wanted surplus countries to adjust by stimulating their economies. U.S. adjustment was deemed out of the question as this would be tantamount to "the tail wagging the dog." However, the Dutch, like many other European countries, feared the inflationary consequences of stimulatory policies in surplus countries and thought that the U.S. should also play its part.

The conflict escalated when surplus countries continued to convert dollars into gold in the expectation that this would force the U.S. to adjust. Toward the end of the 1960s Dutch official reserves consisted of 85 percent of gold and only 15 percent of U.S. dollars. When the U.S. deficits continued to soar, surplus countries were implored to no longer convert their dollar holdings into gold. To this effect a high-level U.S. delegation, including Paul Volcker, visited the Dutch central bank in July 1971 in an attempt to discourage the conversion of two hundred fifty million dollars. When Governor Zijlstra refused, Volcker warned him that he was rocking the boat. Zijlstra's reaction was that if such a small transaction could rock the boat, the boat had already sunk.[12] A few weeks later, on August 15, 1971, President Nixon withdrew gold convertibility, thus initiating the eventual demise of the Bretton Woods system of stable exchange rates.

A New Mission for the IMF

Flexible exchange rates gave large and relatively closed countries like the United States and Germany greater room to maneuver in favor of domestic economic policies. Small open economies were, however, less enthusiastic and the Netherlands became an ardent proponent of regional exchange rate arrangements, like the European Monetary System that was established in 1979. As central bank Governor Zijlstra phrased it, exchange rate flexibility would give small open economies the freedom of a slide as exchange rate depreciation would lead to increased inflation through inflated import prices, in turn leading to further depreciation. Therefore, the Netherlands would continue to advocate rules for internal adjustment, just as it had done under the Bretton Woods system.

In the meantime, international monetary cooperation gradually shifted from the IMF to the G7, which was created as a political forum in the mid-1970s but increasingly focused on economic and financial matters. Although there were successes like the Plaza and Louvre accords in the mid-1980s, international coordination proved difficult as it easily trod on politically sensitive areas. Over these years the Netherlands was a strong supporter of German policies aimed at maintaining price stability. From this, the Netherlands gradually derived the reputation of a hard-currency country.

A new mission for the IMF developed in the wake of the debt crisis in the 1980s and the new membership of former communist countries. Increased emphasis was put on structural adjustment with the aim of reforming domestic policies and creating the basis for sustainable growth. The Fund and the World Bank came to the assistance of countries with large external debts by providing expertise and mobilizing the international banking community as well as official creditors. The enlarged access to IMF's resources—emerging economies received large credit packages—did strain its financing capacity, and the Netherlands played an active role trying to preserve the Fund's monetary character.

Although the IMF and the World Bank try to be nonpolitical and technical,
in practice it is difficult to avoid political influences in their executive boards. The U.S. executive director receives strict instructions from the U.S. Treasury, which in some matters is bound by Congressional legislation, and can veto substantive policy matters. From the American viewpoint, the IMF and the World

Conclusion

As a small, open country, the Netherlands has been a proponent of efficient and effective international monetary cooperation, partly out of fear that the large industrial countries would make a deal among themselves. The Dutch favor a central role for the IMF in discussions on the international financial system and would like the Fund to take a proactive stance. Over the years the Netherlands has maintained a fairly consistent approach toward the Bretton Woods institutions, characterized by a firm belief in international disciplinary mechanisms that promote adjustment.

In contrast, U.S. attitudes vis-à-vis the IMF and the World Bank have changed over time and the United States has increasingly focused on the IMF's financing role in financial crises. As the largest member and the provider of the key reserve currency, it believed that it was entitled to different rules and that it was justified in having its national interest come first. In recent years, the U.S. has increasingly tried to influence policies and force the institutions to align themselves with domestic policy priorities. Also, presidential administrations have taken diverging views, and there have been differences of opinion between the principal agencies involved, such as the U.S. Treasury and the financial establishment in New York. At the same time, it is clear that the multilateral institutions cannot function without continued U.S. support.

Even within the context of the Economic and Monetary Union the Netherlands continues to be an interesting partner for the United States. It is small enough to know that it has to accept international compromises, yet it is financially and economically important enough to make a difference, especially when major countries have disagreements. Among continental European countries the Netherlands has a distinct Anglo-Saxon outlook and it can prove to be an interesting mediating partner with the larger, more regulation-oriented, Rhineland countries such as France and Germany. As the focus in the international discussions has shifted from monetary to financial stability issues, the former Dutch Money Masters now can position themselves as guardians of financial stability.

1 Robert Solomon, *The International Monetary System, 1945–1981* (New York: Harper and Row, 1982), 11.

2 Jan Willem Beyen, *Het spel en de knikkers. Een kroniek van vijftig jaren* (Rotterdam: Donkers, 1968), 158; Jacques Polak, "Financial Relations between the Netherlands and Belgium: 1943 to 1993," in Age Bakker et al., eds. *Monetary Stability through International Cooperation* (Dordrecht: Kluwer Academic Publishers, 1994), 185-186.

3 Keith Horsefield, *The International Monetary Fund 1945–1965*, vol. 1, *Chronicle* (Washington, DC: IMF, 1969), 35.

4 Beyen, *Het spel*, 190.

5 Horsefield, *The International Monetary Fund*, 227.

6 Ibid., 245.

7 Beyen, *Het spel*, 191.

8 Ibid., 183.

9 Jakob Frenkel and Morris Goldstein, eds., *International Financial Policy. Essays in Honor of Jacques J. Polak* (Washington, DC: IMF, 1991), 20-27.

10 Age Bakker, *The Liberalization of Capital Movements in Europe. The Monetary Committee and Financial Integration, 1958–1994* (Dordrecht/Boston/London: Kluwer Academic Publishers, 1996), 37-38.

11 Horsefield, *The International Monetary Fund*, 514. The Group of Ten is composed of the United States, Japan, Germany, France, Italy, the United Kingdom, Canada, the Netherlands, Belgium, Sweden, plus Switzerland (which joined later, making the G10 consist actually of eleven countries).

12 Cited in André Szàsz, *Monetaire diplomatie. Nederlands internationale monetaire politiek, 1958–1987* (Leiden: Stenfert Kroese, 1988), 71.

13 Huib Muller (1988–91), Tom de Swaan (1997–98), and Nout Wellink (2006-present).

14 As the membership of the G20 is mostly the same as that of the twenty-four-member IMFC, which is appointed by the IMF's Board of Governors, its establishment can be seen as another step in undermining the legitimate governing bodies of the IMF.

15 The constituency now is comprised of the Netherlands, Ukraine, Romania, Bulgaria, Israel, Cyprus, Croatia, Macedonia, Armenia, Georgia, Bosnia and Herzegovina, Moldova, and Montenegro.