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**SECOND COMMITTEE, 1450th MEETING**

*Wednesday, 27 September 1972, at 3.00 p.m.*

NEW YORK

*Chairman*: Mr. Bruce RANKIN (Canada).

## GENERAL DEBATE (*continued*)

1. Mr. JOSEPH (Australia) said that in his introductory statement at the 1449th meeting the Under-Secretary-General for Economic and Social Affairs had referred to the link between special drawing rights and development finance, while *The New York Times* of 27 September had published an article indicating the preference of the Ministers of developing countries attending the IMF meeting for a better distribution formula. His delegation had been interested to hear the Under-Secretary-General reiterate that there was no mechanical obstacle to the issuing of special drawing rights on the basis of the link proposal, and that such a step would not necessarily have inflationary consequences. Its own caution with regard to the question of the link would be reduced if it could be convinced that there would be no such consequences. If a preferential allocation of special drawing rights to developing countries was agreed upon, steps would need to be taken to ensure against the issuance of more than were necessary on liquidity grounds. The report of the Executive Directors of IMF on monetary reform[1] contained a full chapter dealing with the link, which must be encouraging to developing countries in that it spoke not of "if" but of "when" such a link would be established. Nevertheless, special drawing rights must be issued solely on the grounds of liquidity, and his delegation wondered whether developing countries would accept a situation in which, after several years, there was for technical reasons a reduction in the number of special drawing rights issued. That question was not a hypothetical one, as IMF was currently considering the volume of special drawing rights it should issue in 1973. Over the past three years the annual average had been $3,000 million, but economists felt there was no justification for such a high figure in 1973 and 1974, and indeed the suggested figures were as low as $1,500 million over the two-year period. If there was to be a link between special drawing rights and development finance, his Government wished to be assured that developing countries would respect the primary need to issue special drawing rights solely on grounds of liquidity and only thereafter to consider their allocation.

2. The last year for which full statistics were available, namely 1971, had been an unrewarding year for the world economy. The underlying reason why growth rates and the expansion of world trade had been lower than in most previous years appeared to be that recessions had taken place in the industrialized market-economy countries, or that their economic performance had been indifferent. Fortunately, developing countries had been able to sustain a respectable growth rate of 5.4 per cent, not far below the target established in the International Development Strategy, and that trend had been accompanied by an improvement in their trading position.

3. If those countries could attain such a growth rate at a time when they were receiving little or no stimulus from the level of economic activity in the industrialized countries, their performance when buoyant conditions returned to the latter countries was likely to be much more spectacular. That was significant, since a recovery was already taking place in the major Western economies, more particularly in the United States, where a real growth rate of 6 per cent was projected for 1972. That development almost guaranteed a return to world boom in 1973, with beneficial effects for the developing countries as well.

4. The fact that the developing countries as a group had consistently outpaced the industrialized developed countries in growth rate every year since 1965 suggested that they had a degree of resilience which was not generally acknowledged, and even the previous predictions of a widening of the gap between rich and poor might be outdated. The gap was of course still wide but, given the interdependence of the world economy, it was more likely to be bridged in conditions where the developed countries were growing alongside the developing than in conditions where there was stagnation in the developed world. A major concern of the United Nations should therefore be to encourage the developed market-economy countries to remedy their own economic situations in the knowledge that stability and expansion in them afforded one of the best guarantees of rapid and unimpeded progress in the developing world.

5. The underlying economic problem facing the developed market-economy countries was inflation resulting less from excessive demand than from cost-push factors, particularly from the tendency for increases in wage rates consistently to outstrip rises in productivity. The result of attempts to tackle that problem by conventional measures, mainly fiscal and monetary restraint, had been to induce recession and unemployment without effecting an appreciable reduction in the rate of growth of inflation. Often, indeed,

[1] International Monetary Fund, *Reform of the International Monetary System: A Report by the Executive Directors to the Board of Governors* (Washington, D.C. 1972).

the curb on economic activity had unfavourable effects on productivity and thus on unit costs. Moreover, there were political limits to the ability of democratic governments to continue with policies designed to restrain economic activity. More often than not, faced with unemployment and recessionary trends, they were forced after a time to relax restraints and even to take active steps to stimulate demand. An inevitable consequence of such action had been to step up inflation. The repeated demonstration of the limited effectiveness of demand management in counteracting inflation accompanied by unemployment had prompted most industrialized countries to resort to a more direct restraint of costs through price and incomes policies. Such policies were difficult to sustain over a protracted period, but in the difficult conditions of "stagflation" there seemed no alternative. Their successful implementation would solve much of the dilemma of policy choice. Governments in the industrialized countries would then be able to pursue expansionary policies without fear of inflation, and the result would be steady growth without the periodic crises which had detrimental effects on industrialized and developing countries alike.

6. Inflation had aggravated, and been aggravated by, the problem of short-term capital flows, which in recent years had reached massive proportions, undermining internal economic management policies and causing severe dislocation in the international monetary system. Attempts to control economies by regulating monetary supply were frustrated by the influx of foreign capital. The policy dilemma arose most clearly with regard to interest rates; high rates imposed in order to restrain inflationary demands might well have the incidental effect of introducing an influx of foreign money, escalating the internal money supply and making it more difficult to control inflation; the problem was at the root of much of the argument in Western Europe about the efficacy of various capital and exchange controls. Capital flows also made the international monetary system unstable. The problem in that case was even greater, because of the vast amounts of money involved—more than $70,000 million in the Euro-currency market alone, a figure which dwarfed the resources available to most nations to defend their currency against speculation. The situation was aggravated by the growth of multinational corporations with financial interests in more than one country, making it very easy for company treasurers to transmit funds from one financial centre to another, either in response to interest rate differentials or as a precautionary measure against rumoured changes in exchange rates.

7. The realignment of currencies resulting from the Smithsonian Agreement of 18 December 1971, together with the adoption of wider bands within which currencies could fluctuate, had temporarily calmed foreign exchange markets. However, developments since June 1972, in particular the intensive speculation against sterling at a time when the United Kingdom's balance of payments on current account was still in surplus, had demonstrated the failure of those measures to create a stable international monetary system. The Under-Secretary-General's view appeared to be that the acceptance of the sterling float revealed that the world on the whole accepted market forces to a greater extent than had been foreseen. His delegation was not convinced that that was the case; the United States dollar, which was the key currency in the system, would probably collapse were it not for the fact that the European central banks continued to pile up unwanted and inconvertible dollars. The system introduced by the European countries in April 1972, designed to narrow the margin within which their currencies could fluctuate against each other, was under equal strain. There was a real danger that the Italian lira might follow the pound in dropping below the famous serpent in the tunnel. The stronger European currencies, as well as the Japanese yen, were bumping the ceiling of the permissible deviation from their central rates. Among the more dramatic of the factors responsible for the renewed speculation against sterling had been the rush of short-term money out of London, peaking to $2,600 million in the third week of June 1972. Earlier, the accumulation of speculative money in the United Kingdom had increased internal money supply by 20 per cent, a dangerous level for a country attempting to control inflation problems.

8. To the extent that movements of short-term capital were interest-sensitive, a greater degree of co-ordination of interest policies among nations was called for to remedy the problem of capital flows. More direct capital controls might on occasion be necessary; indeed, his Government had very recently announced controls to curb the amount of money flowing into Australia. At the same time, however, it had taken measures to make it easier for developing countries to borrow money in Australia, since it recognized that care should be taken not to impede flows of long-term investment capital which were necessary for the promotion of sound economic growth in countries possessing little capital.

9. The other major factor undermining the international monetary system was the continuing weakness of the United States dollar. The basic problem was the continuing United States balance-of-payments deficit, which was paradoxical in that in the past the United States deficit had been primarily responsible for meeting global liquidity requirements. Those responsible for reforming the international monetary system would have to consider what currency would replace the United States deficit in satisfying global liquidity requirements.

10. Conventional logic blamed the breakdown of the system inaugurated by the Bretton Woods agreements on unilateral United States action, including defence expenditure, inflation and the acquisition of foreign companies, which tighter fiscal policies in the United States could allegedly have prevented. His delegation felt that attitude to be unjust; the question was not merely one of burden-sharing, although much needed to be done in that area; it arose mainly from the fact that the Bretton Woods agreements had not allowed for a situation of fundamental disequilibrium in the key economy and the key currency. The post-war

recovery in Western Europe and Japan had inevitably changed their relative economic strength vis-à-vis the United States. Their stronger competitive position should have been reflected in an upwards adjustment of their currency values; but the reverse had in fact happened, with a persistent trend to devalue against the dollar. It was scarcely surprising that the dollar and the United States trade position had moved out of line with those of its major trading partners; what was surprising was that the 1971 crisis had not occurred earlier.

11. Other countries had shown no eagerness to fill the vacuum caused by the suspension of dollar convertibility. The United Kingdom had apparently ceased attempting to reconcile the demands of defending a reserve currency with the obligation to further growth and full employment at home. Japan and the EEC countries had made desperate efforts to prevent their currencies from becoming reserve currencies, and the Swiss had brought down a monetary iron curtain to protect their franc.

12. In view of those past developments, the Committee of 20, currently meeting at Washington to bring about a radical overhaul of the existing system, would not have an easy task. The study of international monetary reform prepared by the Executive Directors of IMF was in many ways unsatisfactory in that it reflected their inability to agree among themselves, and constituted a series of options rather than a set of precise recommendations. A central issue which must be settled was how exchange rate adjustments were to be brought about in future. The Under-Secretary-General had referred to the debate between the academics supporting floating exchange rates and the practical men who favoured fixed parities. It would appear from the IMF study and from recent statements by the Governors of IMF that the idea of completely floating exchange rates had been abandoned; but it also seemed to be conceded that more flexible rules would be required in the future to permit parity changes where they were clearly warranted. A more difficult problem was that of who should bear the responsibility for adjustments. It was not clear whether the onus for adjustment should rest solely on the deficit country, as in the past, or whether the new system should find ways of exerting almost as much pressure on surplus countries to take corrective action. The *World Economic Survey* 1971[2] clearly stated the view that a major source of disequilibrium might be the policies of surplus rather than deficit countries. There was no doubt that the disequilibrium between the United States and its major trading partners would not have developed had the latter been willing to make adjustments, both by increasing measures to liberalize trade patterns and by revaluing their currencies upwards to reflect the increasing competitive strength of their economies. The need to bridge the deficit in the United States payment situation remained fundamental. Recent reports predicted an increase in United States exports, but the dollar devaluation of December 1971 had not yet resulted in material improvement, and concern was felt that the situation might again deteriorate in that the relative buoyancy of the United States economy might lead to heavier imports from abroad.

13. In the multilateral trade talks to be held in 1973 within the framework of GATT, developing countries would be concerned to improve access to international markets for their primary commodities. Australia fully shared that concern since, although it was not a developing country in the conventional sense, it depended on primary and agricultural exports for more than 75 per cent of its foreign exchange earnings. The problems of producers and consumers differed from commodity to commodity, and there was thus no practical alternative to a commodity-by-commodity approach. In commodity agreements, special account must be taken of the needs of developing countries including the least developed among them. The International Sugar Agreement, 1968 might pave the way in that respect, in that it contained provisions designed specifically to benefit developing country sugar producers. Within GATT and through the Kennedy Round progress had already been made in liberalizing trade in manufactures. However, GATT had had only limited effectiveness in reducing barriers to trade in agricultural and primary products. In many cases, indeed, such barriers had been raised, frustrating hopes of a rational pattern of production and trade in such commodities. Accordingly, his delegation welcomed the reference in the joint declaration issued in February by the United States, EEC and Japan, to the inclusion of agricultural products in the negotiations, as well as the statement that they would cover non-tariff as well as tariff barriers.

14. Nevertheless, in the light of the report of the group of high-level trade experts, which had met under the auspices of OECD[3] to analyse trade and related problems in a longer-term perspective, the prospects did not appear favourable. The report made it clear that the major trading nations of the world were totally at cross purposes on the issues of international trade, and nowhere more so than in regard to the crucial question of the treatment of agricultural products. Some understanding appeared to have been reached to the effect that subsidies and other forms of domestic protection to farmers were undesirable and a waste of public money. The need also appeared to have been recognized to harmonize the various protective devices and if possible effect a standstill under which no additional protective measures would be introduced. However, there had been no agreement as to whether agriculture should be eligible for the progressive liberalization of trade which had already been achieved, or was foreshadowed, in relation to industrial needs. Sensitive political and sociological factors were involved, and progress towards removing protectionist agricultural policies could only be slow. However, the world could have hoped for more than an undertaking not to give domestic farming more support than it already had. Even on that aspect, the recommendations

[2] United Nations publication, Sales No. E.72.II.C.2.

[3] Organisation for Economic Co-operation and Development, *Policy perspectives for international trade and economic relations —Report by the High Level Group on Trade and Related Problems to the Secretary-General of OECD* (Paris 1972).

of the group were subject to ratification by national Governments and in some cases by Parliaments. In view of the current signs of a resurgence of economic nationalism, such ratification might not be forthcoming.

15. Australia's trade record was good in comparison with most. At a time when many other countries were strengthening their protective mechanisms, Australia had reduced its tariffs as far and as fast as it could; moreover, those tariff reductions meant a real reduction in protection, since Australia had never developed the system of non-tariff barriers used in many other countries, including some of the more economically successful ones. Australia had been the first country to introduce, in 1966, a system of preferences for imports from developing countries, and was constantly expanding its scope. Over the years it had made efforts to increase trade with the socialist countries, and had concluded trade treaties based on the most-favoured-nation principle with the Soviet Union, Poland, Bulgaria, Romania and Hungary. Further evidence of Australia's liberal trade policy was that for each of the last 10 years its average current account deficit had been $750 million.

16. His delegation agreed with the Under-Secretary-General that the protectionist trend in the chief industrialized nations was the most disturbing element of the current situation. Indeed, many countries exhibiting respectable tariff schedules had fortified their tariffs with an armoury of much more harmful non-tariff devices which could be resorted to when necessary. Particular concern must be felt about the growing protectionism in the United States, where important sectors of the community were urging retaliatory measures in response to numerous deviations from the principle of free trade by the major trading partners of the United States. His delegation did not wish to defend those deviations, since it fully shared the United States concern about the need for a long-term strategy to overcome protectionism in the agricultural area, as well as its concern that the enlarged EEC should not become a highly protective bloc discriminating against the rest of the world. Nevertheless, the general feeling in the United States that its market was open to the world was not correct; the average United States tariffs were about at the same level as those of EEC. Quotas were applied to a considerable percentage of United States imports, including a number of important agricultural imports. The Government applied extensive "Buy American" rules giving preferences to domestic suppliers and had the world's most sensitive anti-dumping legislation. While its grievances might be justified, therefore, the United States too must make an effort to curb protectionist sentiments; the Burke-Hartke Bill, although apparently unlikely to pass the United States Congress in its present form, indicated the dangers which might lie ahead. As the United States Secretary of the Treasury had stated on 26 September 1972 at the annual meeting of IBRD and IMF, the world must avoid a break-up into antagonistic blocs and nations must not seek a refuge from their problems behind increasing walls of protectionism.

17. The close connexion between trade and monetary matters supported the view that both issues should be concluded and negotiated as one package. The United States Secretary of the Treasury had emphasized the link between trade, monetary and investment issues, and had listed a variety of policy responses which countries might take if their payments situation was in imbalance. Those responses included—for deficit countries—devaluation, action to increase internal interest rates and stricter internal fiscal discipline, and—for surplus countries—revaluation, reduction of tariffs and other trade barriers and the provision of greater aid to developing countries. Those suggestions were coupled with proposals for sanctions or penalties against countries which refused to take the necessary action. Although there seemed to be much that was sound in the proposals, the idea of an automatic mechanism whereby changes in exchange rates and other changes would be made on penalty of sanctions might create difficulties for many Governments.

18. The current IMF meeting would also consider questions relating to the future use of special drawing rights, including the proposal for a "link" between the latter and development financing, the role gold should play in the future and what should be done to fund the huge dollar balances already held by central banks outside the United States. The suggestion by the United States Secretary of the Treasury that, as soon as its balance of payments permitted, the United States would be prepared to consider a return to dollar convertibility was interesting and would do much to make monetary reform easier.

19. His remarks had concentrated on the achievement of equilibrium and stability in developed countries because he believed that economic conditions in the industrialized countries could exert a decisive influence on the international system and therefore on the economies of developing countries. Rapid and even growth in the industrial world not only had a stimulative effect elsewhere but eased the policy problems which had hindered developed countries from implementing measures designed specifically to benefit poorer countries. In conditions of buoyancy, it would be much easier for developed countries to assimilate such ideas and put them into effect. All countries therefore had a vested interest in the restoration and preservation of economic health in the industrialized countries.

20. Mr. DE SEYNES (Under-Secretary-General for Economic and Social Affairs) said that he wished to correct any impression of undue pessimism, particularly with regard to the prospects for monetary reform, which he might have given in his statement to the Committee at its previous meeting. Since then, Mr. Schultz, the United States Secretary of the Treasury, had submitted a precise and comprehensive basis for monetary reform in a statement he had made on 26 September 1972 at the annual meeting of IMF and IBRD. The generally favourable reaction to Mr. Schultz's statement indicated that considerable progress had been achieved. For example, there appeared to be agreement on the question of specific

exchange rates and on the need for symmetry in the machinery for adjustment. There also appeared to be a measure of agreement that IMF should have a role to play with regard to the procedures for adjustment. The Australian representative had mentioned the possibility of a consensus on the need to harmonize the control of short-term capital movements. In his view, lengthy negotiations would be required before any basis for an agreement emerged on that exceedingly delicate problem. However the IMF meeting had clearly indicated that there was a real determination to work towards a consensus on monetary reform.

### *Organization of the Committee's work*

21. The CHAIRMAN suggested that the list of speakers in the general debate should be closed at noon on 29 September 1972.

*It was so decided.*

22. Mr. HEMANS (United Kingdom) suggested that the Committee might take up other items on its agenda if faced with the alternative of adjourning meetings early because delegations were not yet ready to make their general statements.

23. Mr. MAKEYEV (Union of Soviet Socialist Republics) felt that a number of delegations would be unable to accept the United Kingdom suggestion. At the present stage, delegations needed time in which to prepare their statements for the general debate and it was important for them to be able to express their views on the whole range of subjects before the Committee. It would not be in the interest of the Committee to interrupt the general debate in order to deal with other items.

24. The CHAIRMAN said that, after consulting the Bureau, he would submit some proposals concerning the organization of work. He agreed that it would be desirable for the Committee to continue with the general debate, provided that that did not encroach on time allocated to other items.

*The meeting rose at 4.10 p.m.*