

OFFICES OF THE WAR CABINET,

GREAT GEORGE STREET,

S.W.1.

18th December, 1941.

As you have been good enough to ask my opinion on one or two points, I feel that I ought to make a brief report to you at this stage.

Keynes has, as you know, greatly simplified his scheme for a bank and has gone very far to meet my criticisms.

There is a rather fundamental point outstanding <sup>about</sup> the precise status of the "bancor" on which I attach a separate note. It is the sort of point which, I should think, should be settled ~~in common council~~ rather than left to Keynes.

There are also one or two frills, which might be cut off. I told Keynes that I did not believe the British Government would in the last resort agree to putting forward a scheme for an interest charge on deposits, however attractive it might be to the theoretical economist, and rather urged him to remove it before the draft went round to Ministers.

I also pointed out that his draft still had in some parts of it the form of a personal statement of opinion and did not yet seem quite to have reached the form of a draft Treasury document. This led him to say a few words about what to the best of his belief would be the procedure.

He thought that Ministers would be asked to decide between two alternatives. On the one hand there would be a statement of how our present system of bi-lateral payments agreements and exchange control might be continued after the war and, indeed extended, so as to be comprehensive. On the other hand there would be his draft with all the objections to it fully set out.

I may say in passing that he did not show a scintilla of dissatisfaction with this arrangement.

I hold, myself, that the former plan ought only to be presented as a last desperate expedient on which we should have to fall back, if all else failed. Perhaps that is in fact the Treasury intention. But in that case, unless there is a third possible plan in existence of which I have not heard, it is clear that the Keynes plan ought to be presented to Ministers as a thoroughly workable and practical plan supported by the full weight of Treasury judgment and as the best plan the Treasury can contrive. This is not inconsistent with setting out explicitly the various possible dangers and difficulties involved in this plan as indeed there must be in any new experiment.

The Ministers and their departmental advisers are bound to be rather at sea in these technical questions of exchange and banking. Unless the new scheme is given a full Treasury blessing, unless it is presented as the best thing that can be devised not merely by the "distinguished economist Mr. Keynes", but by the collective brains of the Treasury, they may have

qualms about giving it their preference. It would be an awkward responsibility to ask them to take.

If the Treasury is not in fact able to give a full and unqualified blessing, then, since the only alternative is highly undesirable and a confession of defeat, it is surely up to them to hammer something out of the material provided by Keynes to which they can give an unqualified blessing, before anything goes round to the Ministers.

It would no doubt be explained to Ministers that it was only intended to put such a scheme to the Americans as an illustration of what we have in mind, and that a number of variants would be equally acceptable; indeed there is something to be said for putting several variants forward to the Americans; but each one should be sponsored by the Treasury as sound and workable.

I now come to the broader question.

In the telegram sent from the Foreign Office to Washington (No. 6914) on December 13th, it is implied in paragraph 4 that we are prepared to enter upon conversations at an early date, and wish to do so before signing the Consideration. But are we nearly ready? Keynes talked of there being still a month before his document need go to Ministers. But a month is a very short time.

This brings me back to the point I made before, that Keynes' bank is quite inadequate by itself as a constructive British proposal for these conversations. I am thinking of course of long-range proposals and not of what we may put forward regarding the immediate post-war problems and exchange control etc.

The bank is inadequate for two reasons:-

1. It is designed to help us in particular. If it were put forward alone, it would seem to the Americans that we had been thinking much more about our own tiresome little difficulties than how we could in co-operation with the Americans introduce more balance into the world economy as a whole. This impression will be all the stronger owing to the great emphasis we keep placing, by unwise tactics as it seems to me, on our own predicted balance of payments difficulties.

2. The operations of the Bank are and ought to be almost entirely automatic and governed by fixed rules. But the Americans will feel, I am sure, with some justice, that some things cannot be put to rights without hard thinking about the particular problems, e.g., the economic future of south-eastern Europe, of colonial territories etc. That is why I regard some plan for an International Investment Board an indispensable corollary of the Bank.

Keynes says that he has looked at my draft and thinks something on those general lines is needed, but has not had time to get down to the details. I attach no special importance to that draft. But I do think it quite essential that we should have something of the sort ready for the "conversations".

Halifax in his telegram 5285 (December 5) refers in paragraph 5(3) to the American anxiety to have discussions about such specific things as capital assistance and nutrition schemes.

I feel that we ought to be prepared with draft schemes, not of course in final form but providing a basis for the conversations, not only on a bank and an investment board, but

also on buffer stocks, commercial relations and agreements, and nutritional standards.

To some extent these fall outside the Treasury. But in every case the crucial difficulty is finance. Who is to find the initial capital, who is to be responsible that it is properly administered, and who is to carry the liabilities incurred from time to time? And how will each and all of the schemes affect the foreign exchange position? These questions are surely very closely tied up with the Bank, the Board and the general financial settlement between the U.S. and the U.K. I imagine it is only the financial skeleton of such schemes that the Americans would wish to have discussed at the conversations.

My comments may be summarised thus:-

1. In view of the possibility of conversations, whatever goes round to Ministers, whether it be the Keynes scheme or some modification of it or something to replace it, should have the full backing of the Treasury as the best possible plan they can devise to meet the post war situation.
2. We ought to have ready for the conversations at least the financial skeleton of schemes not only for an International Bank, but also for an Investment Board, a Buffer Stock Control and a Nutritional Standards Board together with a draft plan for the expansion of world trade by Commercial Agreements, etc.

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## "Bancor"

The name is intended to suggest that this unit of money will have a gold value.

The gold value of a currency is usually fixed by two mechanisms, (i) a buying price at which the currency may be obtained for gold without limit of quantity and (ii) a selling price at which the currency may be converted into gold without limit of quantity.

In the case of the bancor we have the former of these, viz. an obligation imposed on the Clearing Bank to buy gold without limit of quantity. This provision is most valuable, since it gives the two interested countries, the U.S. and the British Empire - and incidentally Russia - an assurance that the new system will not cause a depreciation of gold.

There is no provision for converting the bancor into gold. It is probable that any such provision would ruin the plan.

Thus there is no formal provision for preventing a depreciation of the bancor in terms of gold. Such a depreciation would be entirely innocuous; there is no good economic reason for desiring to prevent it.

On the other hand the name constitutes an announcement to the world that this unit of account is as good as gold, or stable in terms of gold. If this stability is not guaranteed the plain man might regard the name and thereby the whole scheme as a swindle. There is some danger in this.

It can be argued on the other side that though there is no formal mechanism for preventing the depreciation of the bancor in terms of gold, there are two reasons why it would not in fact depreciate.

1. If the U.S. continues to maintain the dollar as a gold standard, the bancor cannot depreciate relatively to gold, so long as the dollar-bancor par remains fixed.

2. Mr. Keynes argues that, even apart from this, the administrative arrangements of his scheme make it extremely unlikely that the bancor would depreciate. The industrial demand for gold is small; it could be met each year from new production many times over; the central banks are not to be allowed to bid for gold above their statutory buying prices. Thus it seems inconceivable that market supply and demand could raise the price of gold above the official buying price. In that case the bancor could not in fact depreciate.

This argument is valid, but some doubt must remain with regard to the size of the demand for private hoarding. It is hoped that confidence in the new currency system will reduce this to a minimum.

Thus it may well be that the bancor is unlikely to depreciate. But is it really proper to give this unit of account a baptismal name, which implies stability in terms of gold, on the basis of probability only?

No doubt much may be said on both sides. I suggest that the name bancor ought not to go forward to Ministers, unless it is the considered view of Treasury officials that the name is a proper one in the circumstances.