

# REFORM OF THE INTERNATIONAL MONETARY SYSTEM WITH SPECIAL REFERENCE TO THE INTERESTS OF DEVELOPING COUNTRIES OF THE COMMONWEALTH

## I INTRODUCTION

### *The Significance of International Monetary Reform*

The 1973 annual meeting of the International Monetary Fund in Nairobi is the first to have taken place on the African continent. It also marks the ten-year anniversary of the placing of international monetary reform on the official agenda. The obstinate persistence of this issue as a preoccupation of governments and financial officials reflects both its complexity and its real importance.

This importance has not always been obvious to the world at large. The problems involved at first appeared theoretical, and then, when the existing international monetary structure broke down under the cumulative strain, the impact on world production and trade was hard to discern. The question was raised whether the enormously difficult task of reconstructing a working rulebook for the international monetary system was necessary for the smooth working of the world economy. In a world of floating rates, the feeling grew, the world economy could perhaps be left in automatic drive.

In the past few months, opinion in world business and political circles on this issue has changed rather dramatically. Serious instabilities in world financial markets have put the vacuum in the international financial order in a new and more threatening light. Calls for progress in the rebuilding of an organized system have been voiced in business circles and by political representatives in many countries. This development is of considerable significance for the task of reform. For this task has long suffered from a lack of sufficient political thrust such as is necessary to override the multitude of technical obstacles and conflicting interests that attend any large task of reconstruction.

International monetary reform has lacked a popular constituency. It is far from certain whether, even now, sufficient political pressure exists to carry a comprehensive and adequate reform to fruition. But the pressure of circumstances has brought a notable movement among all major countries and groups of countries towards a more constructive stance in the official negotiations on a reformed system, in recognition of the importance of attaining a positive outcome.

The significant feature of recent disturbances in international financial markets is that they have occurred in the very largest economies, which had been thought by some to be virtually immune from external shocks under the cushion of floating exchange rates. Smaller countries, and particularly the less developed countries, have always been aware

of their own stake in an ordered and orderly international structure. They have a general interest in a global system that establishes clear-cut rights and obligations, as protection against bilateral and regional relationships in which the balance of bargaining power between powerful and smaller countries is inevitably one-sided.

Besides this general interest, the developing countries have at least three special interests in a reformed monetary order. First, the uncertainty and potential instability of a regime of haphazardly floating rates poses special difficulties for countries that have special ties with a particular financial centre, and that now lack a clear basis on which to maintain their own exchange rate. This is an important problem for a number of Commonwealth countries, and complicates their relationships with neighboring countries whose currencies are linked to different financial centres: the countries involved find themselves in the backwash of the fluctuations of the dollar, the pound and the French franc. Second, developing countries are particularly troubled by the current absence of an international monetary asset with an assured and attractive valuation: in the absence of a suitable store of international value, reserve accumulation by central banks becomes inherently speculative. Third, developing countries have a special interest in the development and extension of an international reserve unit such as Special Drawing Rights. This interest includes, but is not limited to, the persuasive case that exists for a link between SDRs and development aid.

As a result of the establishment of the Committee of Twenty as the forum for the reform negotiations, the developing countries have developed an influential position in the outcome of the exercise. This marks an important advance. In their new capacity as full partners in the bargaining process, the developing countries are not only in a position to safeguard their own interests and to assure that a truly universal approach is taken. They also have the opportunity and the responsibility to consider the requirements of the reformed system as a whole. It has become evident that the benefits of an adequately reformed system are not attainable unless participants in it accept certain restraints on their own freedom of action which they could otherwise pursue. For the developing countries in particular, these restraints are likely to be outweighed many times over by the benefits of a suitably reformed international system. The responsibility that developing countries share with other parties to the negotiations to undertake certain commitments as part of the collective undertaking is therefore in the clear interests of the developing countries themselves.

#### *Design of this Report*

The current official negotiations present all the countries involved with matters for decision that are of considerable intricacy and great

importance. The aim of the present report is to provide countries of the Commonwealth with an additional basis for assessing the implications of these decisions from the standpoint of their own interests, including their interests in achieving a favourable global climate for pursuit of their national objectives.

In these as in all complex negotiations, intensive focusing on the immediate technicalities makes it difficult for the authorities whose decisions are sought – and perhaps still more difficult for those involved in the heat and burden of the negotiations – continuously to view matters on the bargaining table in the full perspective of the substantive problems they are intended to solve. This report is designed to provide such a perspective. It assesses the requirements of a workable international monetary order by reference to the issues under consideration in the official negotiations. But in maintaining the reference point of the goals in view, this report also attempts to direct attention to points at which the drift of the negotiations appears inconsistent with those goals.

The high importance of securing international agreement on this issue brings inevitable pressure for compromise and accommodation among the divergent initial positions held by the various parties to the negotiations. Such compromise and accommodation is inescapable. But it is equally important to step back and assess the proposed arrangements that emerge from such negotiations in terms of the real world problems with which the agreed system will be confronted. Against the damage to international confidence and cooperation that would result from no agreement, there also needs to be weighed the damage that could result from agreement on a new regime that proved inadequate to the task – whether by remaining dormant, or by being implemented and abandoned under pressure, or by having continuous resort to its exceptions and escape clauses. The long-term damage to the world economy and to international cooperation of a failed reform could be very serious.

This report undertakes a substantive assessment of the issues under four main headings. Section II covers a brief general review that relates the new needs of the system to the provisions of the existing regime of Bretton Woods. Section III covers the exchange rate regime and payments adjustment. Section IV discusses the form of reserve settlements and reserve assets, covering in particular the role of SDRs, the problem of foreign exchange reserves, and the link between SDRs and development aid. The final section covers organizational issues on international monetary management at the top level.