IMF and the Federal Republic of Germany in the 1950s

—— "Richesse Oblige" as a Creditor Country——

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Ⅰ. Introduction

This paper centers on the relationship between Germany and the International Monetary Fund (IMF) in the 1950s. Focusing on the linkage between the domestic economy and the international monetary system, this paper elucidates what currency issues Germany faced during the process of its integration into the international monetary system in the 1950s and how the IMF viewed the process and influenced the country's domestic economic policies.[1] As is well known, the establishment of the IMF was decided at the Bretton Woods Conference held in July 1944, and it started its operation in March 1947. However, immediately after its establishment the IMF had to face a situation which differed largely from what the organization had initially envisioned.[2] According to the principles of the Bretton Woods Agreement, the IMF was supposed to engage in multilateral currency adjustments. However, the notion of multilateral approach, which calls for immediate stabilization, multilateralism, and indiscrimination, subsided while the concept of restoring currency convertibility by allowing temporarily exceptional measures was gaining support. The international monetary institution thereafter shifted away from the principles of the Bretton Woods Agreements toward the development of intra-European settlement. This led to the establishment of the European Payments Union (EPU). The IMF, however, faced another crisis at the beginning of the 1950s when the EPU began its operation: the lack of funds prevented the IMF from supplying sufficient international liquidity.

Meanwhile, in October 1950, Germany fell into a balance of trade crisis in the EPU because of worldwide increases in raw material prices resulting from the outbreak of the Korean War in June of the same year.[3] The situation became so unfavorable that the liberalization of imports to the member countries of the Organization for European Economic Cooperation (OEEC) was suspended in February 1951. But, starting in March 1951, Germany's trade balance dramatically improved and started to record excess surpluses (See Figure1).[4] Germany became a member nation of the IMF in August 1952 after it completely overcame the balance of trade crisis. Germany's domestic economic policies now started to integrate into the international monetary system; however, the expansion of exports through the

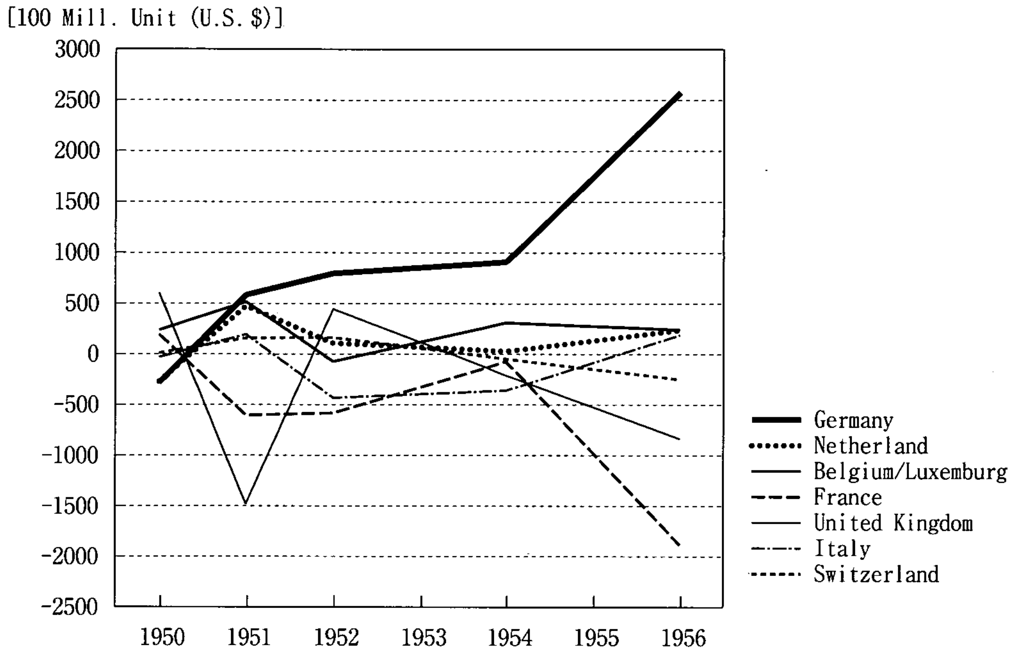

Figure 1 Settlement Position of the EPU : 1950–1958

[Source] Position der Bundesrepublik Deutschland und der übrigen Mitgliedsländer in der Europäischen Zahlungsunion (EZU) 1950–1958, in: Deutsche Bundesbank (Hrsg.), *Deutsches Geld- und Bankwesen in Zahlen 1876–1975*, Frankfurt am Main 1976, S. 349.

European framework was already causing problems at this point. The significant surplus position in the EPU was deemed problematic, and the one-sided expansion of the surplus was taken seriously.[5] With trade surpluses in the EPU resulting in a constant accumulation of foreign reserves, Germany became a pioneer in liberalizing trade, but trade liberalization with the dollar zone had not started when Germany joined the IMF.

So, what was Germany's relationship with the IMF ? Germany neither requested an IMF lending arrangement beyond a set limit nor was presented with lending conditions—the so-called conditionalities. Therefore, there have not been sufficient discussions on the relationship between Germany and the IMF.[6] However, in the case of Germany, the fact that it was a surplus nation rather than a deficit nation caused new currency issues and shed light on problems which led to the collapse of the Bretton Woods system.[7] Once integrated into the international monetary system, Germany, as a surplus nation, started experiencing repercussions from foreign economies to its domestic economic policies. This occurred after the mid-1950s when the principles of the Bretton Woods Agreement came to be realized, and the operations of the IMF started to get on track.

Examining the discussions within the OEEC, this paper first investigates how policies to reduce surpluses were determined for Germany's trade imbalance. Maintaining a cooperative position with the other European nations regarding currency convertibility, Germany decided to use exchange rate policies as a surplus reduction policy through the discussions in the OEEC. Second, this paper elucidates the discussions surrounding the revaluation of the Deutsche mark. The supporting documents used in the following sections are from the IMF Archives, Historical Archives of the Bundesbank, and German Federal Archives. Also, in the discussion on the IMF's evaluations of Germany's domestic economic policies, documents from the annual consultations of the IMF with the federal government and central bank are used.[8]

Ⅱ. Currency Convertibility of the Deutsche Mark

1. Erhard's Views on Convertibility —"The Last Year of the EPU ?"—

From mid 1952, the structure of Germany's trade showed a geographical pattern of surpluses arising from the trade in the OEEC region and deficits from the trade with the dollar zone.[9] Germany's terms of trade improved by approximately 20 percent between 1951 and 1953 because the prices of raw material fell after their worldwide hike due to the Korean War hit a peak.[10] It rapidly rose to 82 percent in 1952, though the liberalization of imports into the OEEC region was resumed in January of the same year (See Figure2).[11] On the other hand, there were still a number of inherent weaknesses in the German position in world trade.[12] For Germany's comeback to the world market, the Federal Minister of Economics, Ludwig Erhard, pushed for the dissolution of the EPU so that it would become an entity with

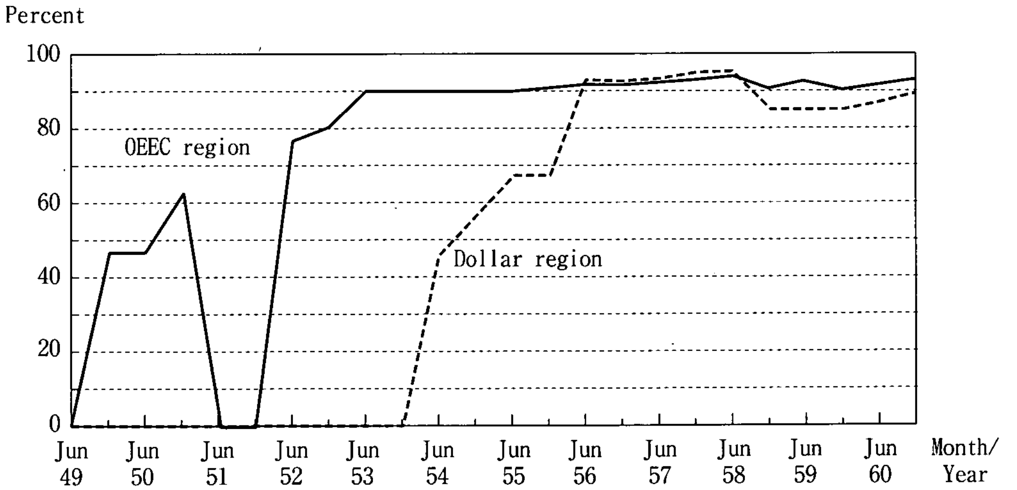

Figure 2 Import Liberalizations: 1949-1960

[Source] Helge Berger, *Konjunkturpolitik im Wirtschaftswunder; Handlungsspielräume und Verhaltensmuster von Bundesbank und Regierung in den 1950er Jahren*, Tübingen 1997, S. 119

limited functions for regional settlements. If the EPU had continued to exist without changes, Germany would have experienced a one-sided increase in its surplus and would have been automatically obliged to provide credits. Erhard feared that credits accumulated in the EPU settlement system might go bad. With a steady increase in German exports, he launched a campaign for the convertibility of the Deutsche mark as an answer to the question regarding how Germany should adjust its surplus in the EPU.[13] If the surplus in the EPU could be converted unlimitedly to dollars, Germany would largely benefit from the potential use of surpluses for raw materials as well as from potential imports from the dollar region.

Erhard pointed out the problems of the EPU settlement system as follows.[14] First, the trade liberalization program of the OEEC lacked strict procedures. He felt that Germany's expansion of the liberalization rate was constrained because under the program it was easy to lower the liberalization rate or stop the process of liberalization based on different situations facing the member countries. In fact, the U. K. reduced its trade liberalization rate from 90 to 61 percent in November 1951 and then to 46 percent in February of 1952. France stopped the process of liberalization during the same period. Second, there were issues with the exchange rate regime. Erhard did not see the compatibility between currency convertibility and the fixed exchange rate regime and sought a ± 5 percent flexible exchange rate system in order to adjust exchange rates among the European currencies. The fluctuation band was set for automatic balance-of-payments adjustments with no influence on foreign reserve levels. Since any level of exchange rate fluctuations was not compatible with the EPU settlement system which presupposed a fixed exchange rate regime, Erhard's proposal implied a resultant dissolution of the EPU or Germany's withdrawal from the union.

Though Erhard attributed Germany's trade surplus to the regional settlement system of the EPU, his radical position met strong opposition not only from other EPU members, but also from the Bank of German States (Bank deutscher Länder). Contrary to his intentions, the continuation of the EPU gained strong support in Germany. The EPU separated itself from the dollar zone and was stably functioning as the framework for European trade. The ability to use surpluses, which were obtained through EPU trade, for raw materials from the sterling region was tremendously important for Germany. Approximately four thirds of Germany's trading partners were in the OEEC region, which highlighted the importance of the European market in reality. The EPU did not hinder the convertibility of the Deutsche mark and thus needed not be dissolved. As with the dollar region, Germany's exports to the region remained stagnant due to the U. S. tariff barrier and import policies, which made it difficult for Germany to withdraw from the EPU.[15] Erhard regarded the surplus in the EPU as being equivalent to dollars gained ; however, it was the existence of the EPU settlement mechanism that ensured the constantly increasing German foreign reserves.[16]

Germany chose to make policy adjustments with the U. K., stayed with the EPU, and avoided the breakdown of relationships with France despite the fact that Germany could realize convertibility by itself. Germany continually took steps toward convertibility after April 1954. It established a freely convertible DM account as well as a partly convertible DM account, which were transformed into the liberalized capital DM account in September 1954. With surpluses, Germany held a decisive position as a creditor in the EPU. Thus, it attempted to expand the range of gold or dollar settlements of the EPU, establish a more extensive multilateral system and restore convertibility. In this process there were intense arguments exchanged between Germany, a surplus nation, and the U. K., a deficit nation, regarding convertibility.

In May 1953, Erhard and Franz Blücher, Vice-Chancellor of Germany and the Federal Minister for Matters of the Marshall Plan, were invited to London by Richard A. Butler, British Chancellor of the Exchequer, and Peter Thorneycroft, President of the Board of Trade, to discuss currency convertibility.[17] At the London conference, Erhard argued the necessity of European initiatives toward convertibility in order to induce support from the U. S..[18] He was more optimistic than any other person and believed that the IMF would provide additional financial support to solidify the stability of the European currencies. However, the IMF did not take an initiative even at the annual meeting held in Washington, D. C. in September 1953, and its inaction disappointed member countries.[19] The activity of the IMF was low-key even in terms of the annual quota ratio. Many of the IMF loans had actually been denominated in dollars since it had begun its operation. Moreover, the amount of loans was declining after the launching of the Marshall Plan, and the IMF was facing a more serious crisis. In November 1953, Erhard unofficially visited the U. S.. The occasion led to the meeting between Otmar Emminger, German Executive Director at the IMF, and Frank A. Southard. Jr., U. S. Executive Director, on the role of the IMF in restoring convertibility.[20] At that time, the IMF could not provide financial support of approximately 50 billion dollars—the amount needed by the European nations according to Emminger's estimate. Ivar Rooth, IMF Deputy Managing Director, stated that Erhard sensed the IMF as incapable of providing financial assistance necessary for the European nations, so it was unclear to Erhard which organization could responsibly take on the issue of convertibility.

Erhard looked forward to an early realization of convertibility at consultation meetings with the IMF immediately following Germany's membership. As to how the IMF evaluated the convertibility of the Deutsche mark, a discussion was held in February 1954 at the annual IMF consultation for 1953.[21] The IMF staff led by Irving S. Friedman, the Director of the Exchange Restriction Department, and John M. Stevens noticed Erhard's aspiration for currency convertibility and asked Germany's views on the convertibility of the Deutsche mark. The German representatives pointed out that the focus was on convertibility for the domestic residents. When asked about the possibility of achieving the 100 percent convertibility for both residents and nonresidents within a relatively short time period, they explained that the status quo did not allow for an immediate achievement, but that Germany would proceed comprehensively taking into consideration issues including the liberalization of imports to the dollar region and capital movements as well as the abolition of bilateral settlement agreements. Noting that if surpluses in the EPU could be settled 100 percent in gold or dollars, Germany would not need to worry about trade imbalances in the dollar or OEEC zones, the staff from the IMF reaffirmed the tight connection between the surplus position in the EPU and the liberalization of imports to the dollar region.

2. Discussions in the OEEC —The Mark versus the Pound—

Germany's trade surplus originated from trade imbalances within the European nations. Although Germany was experiencing trade deficits against the dollar region, it had surpluses against the European nations and was in the midst of a prudent move toward import liberalization. As of April 1953, its liberalization rate for imports from the OEEC regions had already reached 90.1 percent; however, it began liberalizing imports from the dollar region at the 51.9 percent level in February 1954 (See Figure2).[22] Even though trade with the dollar region drastically expanded in 1955 with a 61 percent rise in imports and 30 percent increase in exports, deficits against the dollar region were ultimately covered by surpluses against the European nations. However, the chronic dollar shortage started to show gradual changes around the mid 1950s. Germany had sufficiently accumulated foreign reserves, and the fact that its balance of payments showed one-sided deficits against the dollar region did not have as much importance as it did in the beginning of the 1950s. The liberalization of imports from the dollar region had also rapidly expanded, with its rate reaching 92.7 percent in June 1956 (See Figure2).[23] At the annual consultation for 1956, the IMF concluded that Germany no longer needed import restrictions.

The bipolar phenomenon in which a large gap separates surplus nations from deficit nations within the EPU was for Germany an urgent issue related with the convertibility of the Deutsche mark.[24] Contrary to Germany, the U. K. and France had deficits not only against the dollar region, but also in the EPU (See Figure1). That is, both nations suffered double gaps—one against the dollar and the other against the Deutsche mark. The bipolar phenomenon in Europe meant that a problem which would lead to a crisis for the IMF system after the 1960s had already surfaced.

Erhard engaged in the readjustment of exchange rates in order to correct trade imbalances within the European nations. The readjustment meant a de facto revaluation of the Deutsche mark—that is, a devaluation of the British pound and French franc. On June 14, 1956, Erhard published an article entitled "Konjunktur und Wirtschaft, Außenhandel keine Einbahnstraße" in Die Zeit in which he argued that a conference on international currencies should be held at the level of the OEEC or IMF in order to adjust multilaterally exchange rates of the European currencies.[25] His claim can be summarized as follows. Germany's trade partners were not pleased with the increase of its trade surplus, and there was discussion of eliminating Germany's excessive surplus. It was, however, the limitation of the settlement capacity of the EPU that should be blamed, not Germany. Germany was expected by the trade partners to offer better opportunities with freedom in its market, implement a good-creditor policy, and reduce their deficits. Exchange rates were not adjusted (despite the large differences among the price levels and trade balances of the European nations). The claim made by Erhard induced speculative activities based on the expectation of a potential revaluation of the Deutsche mark, and Germany's trade surplus rose further.[26]

Erhard provided Harold Macmillan with an additional new proposal for exchange rate adjustments in July 1956, ahead of the OEEC meeting of ministers starting on the 17th of the month. Arguing that the stable Deutsche mark currency should maintain its parity, that the weak currency pound should be devalued, and that if the currency of a deficit country was not devalued, the fluctuation band of the exchange rate should be expanded to ± 5 percent, Erhard demanded that the U. K. devalue the pound or temporarily float the exchange rate.[27] The British government had already proposed the introduction of a ± 1-3 percent band to the exchange rate in March 1955. Since Germany had rejected the proposal, the discretionary statements by Erhard were surprising. The U. K. declined the proposal for a reason that such devaluation would induce speculative activities against the pound and accelerate the inflow of foreign exchange into Germany. In his explanation at the OEEC meeting, Macmillan mentioned several points: Germany's trade surplus was expanding at an unimaginable scale; its share in the total credits of the EPU would not reach even 80 percent at the end of 1956; it was capable of solving the problem by an increase in its EPU credit ratio, pre-maturity debt repayments, and capital exports; if it allowed little inflation adjustments, it could lower the interest rate and could ultimately revalue the Deutsche mark; and it was the only nation considering adjustments of exchange rates. Despite persistent opposition by Erhard, the exchange rate issue was viewed as an area solely managed by the IMF, and no concrete discussions were held at the OEEC meeting. Since the IMF Executive Board actively supported devaluations of the European currencies in September 1949, the IMF and OEEC had been at odds with each other. Also, it was true that the IMF did not possess sufficient power to take on new reforms.[28]

3. The Limit of Germany's "Good Creditor Policy"

The surplus position of Germany was one of the main themes at the OEEC meeting and came to be widely recognized as Germany's dilemma. Germany became a surplus nation against all non-sterling EPU member nations, notably against the Benelux and Switzerland.[29] In spite of Erhard's arduous explanation of Germany's efforts toward balanced external payments and the responsibility of the deficit nations, Germany's excessive surplus became the target of blame (See Figure1).[30]

In November 1956 at the OEEC meeting of ministers, Erhard made an announcement regarding the surplus position of Germany: the price level in Germany was maintained at relatively low levels; there was an enormous inflation pressure although it was not as strong as other nations'; and this in turn meant that Germany was forced to export capital despite the domestic need for capital and an appropriate level of interest rate corresponding to the need.[31] In response, with a reason that surplus nations were also responsible for trade imbalances, Germany was asked to promote small-scale measures to reduce its surplus, such as the expansion of import liberalization, decreases in tariff rates, and capital exports. Contrary to Germany's intentions, the OEEC started seeking to solve trade imbalances in the EPU by multifaceted actions within the existing framework.[32]

The trend of Germany's surplus in the EPU showed further expansions in the second half of the 1950s. At the OEEC meeting for financial stability, the discussion on trade imbalances reached its peak. Alfred Müller-Armack, chief of the planning section of the Federal Ministry of Economic Affairs explained Germany's position: Germany's surplus was a result of the strong inflationary tendency of the deficit nations, and there was no shared responsibility for Germany; exchange rate adjustments would be an effective solution; the promotion of capital exports were not appropriate due to German economic policies; the problem of trade imbalances, let alone Germany's capital market conditions, interest rate level, and difficulty in acquiring capital, could not be solved fundamentally without a 180 degree shift in economic policies of the deficit nations with ongoing inflation; nations with large deficits must suppress demand by domestic economic policy measures in order to eliminate Germany's surplus position; and Germany, in fact, had tried as many measures as it could to correct its trade imbalances, such as reductions in tariff rates of an average of 25 percent, import liberalization, the simplification of import procedures, the abolishment of export promotion, and pre-maturity debt repayments, which clearly made significant contributions. Germany, however, again received severe criticism from other European nations at the OEEC meeting for financial stability.[33] The U. K. and Scandinavian nations attacked Germany's position, pointing out that it neither sufficiently implemented measures to correct or lessen trade imbalances nor attempted to stimulate its domestic consumption or investment.

The criticisms against Germany differed in their intensity, but had common aspects shared among other European nations. But, not all measures requested of Germany could demand an immediate response. This applied to exchange rate adjustments, but not to an intentional increase of the price level. At the time, it was widely recognized that the adjustment of exchange rates was effective in correcting trade imbalances. Also, it was pointed out that if Germany continued its monitoring over rising prices, the stability of the price level would be unconditionally maintained and would necessarily lead to enormous surpluses as long as no change was made to exchange rates. Thus, the revaluation of the Deutsche mark was entrusted to Germany's judgement.[34]

Ⅲ. Debate over the Exchange Rate System

1. Germany Imports Inflation from Abroad

Great progress was made toward the restoration of convertibility with the European Monetary Agreement signed in August 1955. The ratio of gold or dollar settlement in the EPU greatly increased after 1955 from the original 25 percent to 75 percent, and the system came to more multifaceted. Though the path to the restoration of convertibility became clearer, the trade imbalances of Western European nations increased their severity. Emminger focused on the relationship between the fixed exchange rate regime and changes in the price level for the first time in June 1956, questioning if the situation in Germany might be what an IMF Article calls fundamental disequilibrium. Germany's monetary policy faced an internal vs. external balances dilemma which was characterized by the impossibility of the simultaneous attainment of balanced international payments and domestic stability under the fixed exchange rate regime. An incompatible situation emerged in which, on one hand, the domestic economic condition required a contractionary policy to dampen the overheating economy, while on the other hand, the external economic conditions called for an expansionary policy to balance payments. As long as Germany's currency maintained a relatively stable value, its major trade partners, the U. K. and France, experienced severe inflation. However, the Bretton Woods system did not possess a mechanism for instantly adjusting exchange rates in response to such inflation differentials. If this situation were to continue, German exports would expand further, and the U. K. and France would, in contrast, experience low export growth because of the overvalued pound and franc, which in turn would lead to Germany's chronic trade surpluses.[35]

On June 6th, 1956, during a seminar at the IFO Institute of Economic Research, Emminger expressed his great fears regarding the impact of Germany's current account surplus on its domestic prices and stated that Germany might be importing inflation from other nations with trade surpluses and the inflow of foreign currencies resulting from exports.[36] The statement was largely reported in the economy section of Süddeutsche Zeitung published on the 7th.[37] At the same time, active discussions started both domestically and internationally about the possibility of a revaluation of the Deutsche mark as a defense measure against imported inflation. Emminger's proposal at the seminar mentioned the promotion of capital exports, early repayment of debt, and reductions of export promoting measures as defense measures. He suggested these measures to Wilhelm Vocke, President of the Bank deutscher Länder, but Vocke rejected the idea of imported inflation and did not take Emminger's claims seriously. Vocke did not hold the view that the dilemma between the domestic and external balances would cause excessive domestic liquidity, making control difficult to achieve.[38]

Emminger supported the idea of an immediate revaluation of the Deutsche mark. A revaluation was theoretically effective as an adjustment measure in a surplus country; however, as described in the following, a domestic conflict—a strong opposition from the industrial and banking sectors which were major actors in exporting—was anticipated. Also, even though there were already countries which devalued their own currency, no country had ever experienced a revaluation in order to defend the stability of the domestic value of its own currency from the influences of external economies.[39] In the world of international finance, a view that the exchange rate was an untouchable area remained strong due to the experience of competitive devaluations during the 1930s. The emphasis on the fixed exchange rate suppressed the adjustable aspect of the exchange rate. Similar views were tightly held not only by Vocke, but also by many executives inside the Bank deutscher Länder.

A secret executive meeting was held at the Bank deutscher Länder on December 12th, 1956 to discuss Emminger's proposal for a revaluation. Emminger prepared an internal document titled "Germany's Surplus Position and Exchange Rate Policy".[40] He aggressively made the following arguments for the revaluation of the Deutsche mark as the sole defense measure in a situation where there was domestic stability of the currency. (1) Sooner or later, a revaluation of the Deutsche mark would be unavoidable in order to sustain the domestic stability of the currency. (2) To avoid repeated monetary policy failures, a revaluation must be done immediately with the appropriate rate of 6-8 percent. (3) There would be numerous benefits in adjusting the exchange rate. The new exchange rate was to be determined by setting a temporary transitional period and based on the resulting change in its parity. For example, a margin of ± 6 percent was to be established until the rate converged to its new level.

As Emminger himself expected, the argument for a revaluation of the Deutsche mark met strong opposition which included the following.[41] (1) The Emminger proposal would set a wide fluctuation margin, but would not ultimately change the parity. (2) The Bank deutscher Länder should emphasize the coordination with other nations, not a revaluation of the Deutsche mark. The key was whether the deficit nations would devalue their currency. (3) In case the Deutsche mark would be revalued, it would be important how the U. K. and France would receive the situation when they were pressured for debt reductions. In both nations, the pressure for the implementation of domestic economic policies to reduce debt and for exchange rate adjustments should not be lessened. (4) The exchange rate was a fundamental basis, an inviolable area which should not be modified. Alternative measures for balancing external payments such as import promotions, the abolishment of export promotions, and capital exports, should be taken instead.

Emminger was forced to agree to refrain from supporting a revaluation of the Deutsche mark in order to prevent excessive currency speculations. He well understood the importance of cooperating with deficit nations in solving external payment imbalances and emphasizing the devaluation of their currency since he himself held a view that deficit nations lacked internal balances, and that they, rather than surplus nations, should make initial adjustments. The notion that deficit nations had a greater obligation to make adjustments than surplus nations had often been repeated in the discussion on revaluating the Deutsche mark. Vocke considered that the relation between the Deutsche mark and the dollar was normal even if some adjustment was needed for the exchange rate between the Deutsche mark and the franc, and worried about possible confusions caused by a sole revaluation of the Deutsche mark. As mentioned above, Germany covered the deficits against the dollar region using its surplus against Western European nations, and the sole revaluation of the Deutsche mark was considered to bring about serious damage to its balance of payments against the dollar zone. The Emminger proposal was suppressed by discussion at the executive meeting. Emminger fiercely resisted ; however, Vocke expected that a rise in money supply caused by the inflow of excess liquidity, social reforms, wage hikes, and a reduction of the government surplus would lead to an expansion of the German economy, which would, in turn, result in less inflationary pressure.

2. IMF Annual Meeting for 1957 in Washington, DC —Jacobsson Against Germany—

The conflict between internal and external balances escalated in 1957 due to speculative currency inflows. The international currency speculations were based on the anticipation of a revaluation of the Deutsche mark and a devaluation of the pound and franc. A revaluation of the Deutsche mark would certainly bring external payments to balance. However, it faced great domestic opposition. The federal government along with the Bank deutscher Länder strongly opposed the revaluation. Erhard was the only minister who believed in the necessity of exchange rate adjustments. But, contemplating discussions with West European nations and facing strong opposition from Federal Chancellor Adenauer, Erhard himself gradually had to suppress his intention to implement a revaluation.[42]

The industrial sector, which was anxious about losing a competitive edge in the export markets, and the banking sector, which had close ties with exporting manufacturers, were against a revaluation of the Deutsche mark. The opposition was led by Hermann J. Abs of Deutsche Bank, Fritz Berg, chairman of the Bundesverband für deutschen Industrie, and Robert Pferdmenges, chairman of the Association of Private Banks, who were all powerful economic advisors of Adenauer.[43] In the summer of 1957, the federal government and the German Federal Bank (Deutsche Bundesbank) jointly denied the possibility of a revaluation of the Deutsche mark in order to pacify the situation.[44] They repeatedly emphasized that the relationship between the Deutsche mark and the dollar did not need adjustment, with all economic conditions considered.[45]

Germany and the U. K. announced emphatically the maintenance of the existing exchange rate at the IMF annual meeting held in September 1957. The summer of the same year saw pressure on the pound resulting from intense currency speculations in the foreign exchange market based on the expectation of a revalued Deutsche mark and a devalued franc. Such a phenomenon had not been seen before an annual meeting since the establishment of the IMF. The IMF had increased its activities after the financial assistance following the Suez Crisis of 1956.[46] The international finance world became tense, anticipating that the annual meeting would become "the most eventful since 1949".[47] To stimulate the atmosphere for a revaluation of the Deutsche mark, Emminger pointed out issues involving the adjustment of exchange rates appropriate to the economic reality.[48] In his scenario the IMF would not be the leading authority, but each member nation would have to take initiatives independently. This had not been even discussed at the annual meeting. In such circumstances, Emminger argued for floating exchange rates, but due to the cooperation between Germany and the U. K., the annual meeting ended "with an unexpectedly dramatic conclusion" supporting the IMF-led recovery of trust in the existing exchange rate and the elimination of speculative activities against the Deutsche mark and pound.[49] This result reflected the great influence of Per Jacobsson. He had been director of the financial economics section of the Bank for International Settlements and became the third Managing Director of the IMF in December 1956. He was the person sent to Germany in October 1950 and contributed to the continuation of trade liberalization by implementing the EPU special credits. In the midst of facing severe criticisms against the weakening of the IMF, he successfully initiated numerous standby agreements and put the organization on the path to its resurgence after he started his office.[50] He was concerned about the potential uncertainty caused in the international monetary system by a revaluation of the Deutsche mark and expressed his opposition to it. He also suggested the possibility of the reversal of the trend seen in trade balance in case of changes in German domestic economic conditions.[51] Jacobsson pointed out that fluctuating exchange rates would create problems for trade, in particular long-term contracts, and increase the danger of speculative movements of funds.[52] While he insisted that the postwar inflation was soon over, Emminger did not concur.[53]

Executives of the IMF told Germany (1) to utilize the annual meeting to maintain the status quo in the Deutsche mark exchange rate and (2) to show again its commitment to maintaining exchange rates announced jointly with the U. K. in August 1957. The U. K. also approached Germany with an intention to make coordination compatible with the commitment.[54] The agreement between the two countries reflected the intention of the IMF that their coordination should avoid causing new distrust against the exchange rate of the counterpart. Even after the announcement of the agreement, there were still opinions questioning the benefit and credibility of the agreement.[55] But, Jacobsson emphasized that the agreement was not superficial by showing an example of a policy coordination effort in which Germany reduced the interest rate on September 18th from 4.5 to 4 percent and the U. K. the next day increased its interest rate from 5 to 7 percent in an attempt to counterattack the international speculative pressure on the pound resulting from the devaluation of the franc immediately prior to the annual meeting.[56]

In the 1957 annual consultation, the IMF was anticipating that an increase in Germany's imports originating from an expansion of its domestic economy would stimulate international trade, and that its capital exports would lead to balanced growth of the world economy.[57] In the eyes of the IMF, the position of Germany changed from a surplus nation in Western Europe to a nation expected to contribute to international trade. The conflict between the domestic and external balance disappeared because of a decline in worldwide economic activity. The speed of export growth in Germany declined due to an inflation slowdown and the contraction of domestic demand in deficit nations.

Ⅳ. Currency Revaluation of the Deutsche Mark in March 1961

1. IMF Annual Meeting for 1960 in Washington, DC
—Capital exports as "Richesse Oblige"—

The conflict between the domestic and external balances resurfaced in 1959. As was the case in the mid-1950s, Germany experienced economic growth led by construction investments. In 1960, the GDP growth rate reached 9.0 percent, and the unemployment rate declined to as low as 1.3 percent. Due to the above-full-employment condition, the total wage growth rate rose from 5.4 percent in 1959 to 9.3 percent in 1960. The Bundesbank, once again, had to face the dilemma of having increases in wages and prices and the expansion of a balance of payments surplus.

The conflict between the domestic and external balances of the 1960s was different from that of the 1950s.[58] Speculative currency inflows in the second half of the 1950s comprised European currencies such as the pound and franc. However, an inflow of the dollar started in the 1960s. The dollar inflow was accelerated since, in addition to preferences away from the dollar, the German interest rate was higher than the U. S. interest rate by as much as 1 percentage point. The reemergence of the conflict between the domestic and external balances completely defeated the view that it was a temporary phenomenon. The possibility of a revaluation of the Deutsche mark started to be reexamined.

In January 1960, Emminger again posed a question at an executive meeting of the Bundesbank. He pointed out the possibility of a wage-price spiral in an internal document titled "Examination of Currency Policies".[59] Jacobsson emphasized the end of postwar inflation; he concluded that the period of malfunctioning credit policies caused by the post-World War II excess liquidity had come to an end thanks to stabilized wages and prices in the U. S. and the tighter economic ties among industrialized nations. Emminger, however, squarely rejected the end of postwar inflation. Observing that the longer the sustained excess demand, tension in the labor market, and potential inflation lasted, the greater their impact on prices, he argued the following points. (1) The effective measure taken to solve the existing conditions was exchange rate adjustments. Fiscal policies could not offer flexible solutions. (2) Tightening of the domestic economy through contractionary measures would lead to export growth. As a result, the problem of surpluses in foreign exchange balances would become more serious. (3) Unlike the 1956-57 period, differences in inflation across Western European nations were not important in the discussion on imbalances. The problem of Germany's surplus this time would require the consideration of the U. S. deficits. The dollar was a major currency, and a voluntary adjustment with its devaluation could not be expected.

(4) A decision must be made immediately whether to accept adjusted inflation or a revaluation of the Deutsche mark. (5) Though multilateral adjustments of exchange rates were desired, a realistic solution would be a sole revaluation of the Deutsche mark. (6) As to the degree of the revaluation, it was to be a conservative number of $1 = 3.90DM, a 7.7 percent revaluation, taking into account the need to protect domestic industries. The president of the Bundesbank Karl Blessing was determined to oppose such revaluation. But, even a powerful director like Eduard Wolf started to recognize that the conflict between the domestic and external balances was not a temporary problem.

In June 1960, the executive board of the Bundesbank launched "a credit policy broadside". Under the perfectly free system of capital transactions, is it possible to realize domestic stability without revaluing the Deutsche mark ? The implemented measures were: (1) an increase in the interest rate (from 4 to 5 percent) as well as in the Lombard rate (from 5 to 6 percent), (2) an increase in the minimum reserve ratio and the reduction borrowing from the discount window, (3) a zero interest rate for nonresident savings (as a protective measure against foreign funds), and (4) coordination between the Bundesbank and financial institutions—the so-called "Blessing Million".[60] The liquidity policy implemented in the fall of 1959 did not show sufficient effects until the spring of 1960. The implementation of the policy attracted great anticipation when liquidity reserves were further expanding due to currency inflows.

However, the final bet by the Bundesbank eventually failed because of a tragic coincidence of the implementation period of a contractionary policy in Germany and an expansionary policy in the U. S.. The U. S. shifted toward an expansionary policy with two 0.5 percent interest rate reductions. A large interest rate differential emerged as the U. S. reduced its interest rate from 4 to 3 percent only one week after Germany raised its interest rate. Sensing a potential crisis, the U. S. requested Germany to increase its capital exports and to financially contribute to the expenses of the stationed military forces as a measure to solve payment imbalances. Facing domestic and international pressure, the federal government provided financial assistance to developing nations in an attempt to avoid a revaluation of the Deutsche mark.[61] Aid worth 2 billion DM was urgently prepared by borrowing from the federal and state budgets, the Marshall Plan fund, and German industries.

At the IMF annual meeting in September 1960, a revaluation of the Deutsche mark was not even mentioned following Jacobsson's direction.[62] He considered that the revaluation by about 6 percent proposed by Emminger was too small to have an impact on the settlement position and estimated that a 15 percent revaluation was necessary to eliminate imbalances. He also expected that new speculative currency inflows would still result from a revaluation and judged no intervention in the foreign exchange market as a preferred method. For

Jacobsson, stable exchange rates were the main consideration, and the shift toward a flexible exchange rate regime was deemed extremely dangerous. He was committed to maintaining and strengthening the existing order in international currencies, which was seen to be too conservative by the proponents for the creation of a new international order, such as Emminger.[63]

The German surplus was also criticized at the IMF annual meeting, and Germany was strongly requested to perform "Richesse Oblige".[64] The expanding foreign reserves in Germany were regarded as a disruptive force for international cooperation, and Germany was requested to take a share in international contributions through capital exports. Jacobsson suggested Germany solve the issue by an expansionary domestic policy along with a pre-maturity repayment of debt and financial assistance to developing nations. Jacobsson's statement that Germany should consider conditions of deficit nations and allow controlled inflation met with widespread criticism in Germany, so he suggested Germany compromise with inflation.[65] But, the annual meeting was full of Jacobsson's influences. In fact, prior to the meeting, not only the U. S. delegates, but also the delegates from European nations had been advised not to be sympathetic to Germany's effort for revaluation and to press it for capital exports.

2. Judgement of the Mark's Revaluation

In October 1960, the federal government decided to maintain the status quo for the Deutsche mark exchange rate, following the general statement of the IMF annual meeting. On the other hand, the credit policy broadside failed, which revealed the incapability of the Bundesbank monetary policies.[66] If the Bundesbank surrendered, it would mean the failure of Germany's domestic stabilization policies and the progress of controlled inflation. With no possibility of a revaluation of the Deutsche mark, the Bundesbank had to move toward an expansionary policy compatible with external payments. It placed a focus on reducing interest rate gaps against other nations and on discouraging the currency inflows. On November 10th, the interest rate was lowered to 4 percent and the minimum reserve ratio abolished. This declaration of surrender by the Bundesbank caused a serious conflict with the federal government. Erhard and Federal Minister of Finance, Franz Etzel, persistently supported domestic stability and directly confronted the Bundesbank. The conflict became a turning point where the likelihood of a revaluation jumped. Erhard made clear his intention to protect domestic stabilization policies with a revaluation.[67] For the stabilization of the currency value, Germany had nothing but a revaluation of the Deutsche mark.

The federal government finally decided to revalue the Deutsche mark on February 28th,

1961. But, the revaluation was kept at the smallest possible level. Erhard and Emminger considered a revaluation by 7.7 percent; however, Adenauer, anticipating support from the industries in the federal election of 1961, reduced it to 5 percent so that the exchange rate now became $1 = 4.00DM. The revaluation received a mixed reception: some were surprised at its implementation with consideration given to its impact on the domestic industries while others saw it favorably as a contribution to the international community. On March 3rd, Emminger went to Washington, D. C. at the direction of Erhard. Before his arrival, Southard Jr. and David Pitblado along with Friedman, Joseph Gold, the Director of the Legal Department, Jacques J. Polak, the Director of the Research and Statistics Department, and Gabriel Ferras, the Director of the European Department, were preparing for a Board meeting and kept their eyes on the degree of the revaluation.[68] Jacobsson repeated his long-held view that a small revaluation by less than 7-8 percent would distort foreign exchanges. Southard Jr. also stated a revaluation by less than 8 percent would be meaningless.[69] The IMF Executive Board unanimously accepted the 5 percent revaluation of the Deutsche mark since it was within the allowable range of 10 percent set in the Articles. The Board, however, pointed out that the revaluation was too small.[70] Moreover, the Board predicted that the revaluation would generate an expectation for a series of future revaluations even though it had a certain level of positive impact on uncertain Deutsche mark exchange rates.

On March 5th, 1961 the federal government and the Bundesbank jointly announced the revaluation of the Deutsche mark. Blessing pointed out Germany's contribution in his speech. At the same time, he mentioned difficulties involving the decision: the Bundesbank had long resisted adjusting exchange rates and would like to ask for generous understanding of its decision; and for a central bank, the parity of its nation's currency had been sacred and inviolable, and its adjustment was an ultimate measure allowed only in a situation where any other measure had failed to provide a solution. Erhard emphasized that the federal government had recognized the stability of the currency value as the primary policy from the beginning and would not hesitate taking decisive measures in order to achieve it.[71]

For the U. S., discussions about direct German measures to help offset the U. S. balance of payments deficits were a higher priority; revaluation should not be used as a substitute for these measures.[72] U. S. Secretary of Treasury, Douglas Dillon, said that he thought the Germans should revalue by at least 10 percent, although the U. S. government did not openly pressure the federal government on this issue.

V. Conclusions

Germany pushed for the liberalization of exchange rates to integrate its newly constructed production structure into the system of international specialization in the face of foreign competition. During the 1950s, the objective of liberalizing trade and exchange rates shifted to an attempt to balance the current account.[73] The export expansion which became a driving force for economic growth for Germany concentrated against European nations, and Germany experienced an accumulation of trade surpluses. The dramatic improvement of trade balances and resulting accumulation of surpluses as well as the conflict between internal and external balances caused by the inflow of foreign exchange made the administration of domestic economic policies tremendously difficult and created great confusion. In the beginning of 1952, Germany's focus was on correcting the concentration of exports against European nations and on restoring convertibility to expand trade with the dollar regions. Openly criticizing regionalism, and even suggesting a withdrawal from the EPU, Erhard launched a campaign for convertibility, but, at the same time, Germany's increasing foreign reserves was attributed to the very existence of the settlement mechanism of the EPU. The negotiations with the IMF revealed that Germany's effort toward convertibility had to face issues such as the expansion of import liberalization for the dollar region, abolishment of bilateral settlement agreements, and liberalization of capital movements. There was a tight link between the surplus position in the EPU and liberalization toward the dollar zone. In 1956, however, the liberalization of imports from the dollar region had expanded. The IMF was confident that the German government would continue policies designed to stimulate capital export, particularly on a long-term basis, and that sustained growth of the German economy would ensure a strong demand for imports and contribute to a renewed expansion of world trade.[74]

The integration into the international monetary system meant that Germany had to seek measures for adjusting its surpluses. The trade surpluses led to a deflationary automatic adjustment as long as deficit nations did not devalue their own currency, and to an inflationary adjustment without a revaluation of the Deutsche mark. There were discussions whether a condition that the IMF Articles called "fundamental disequilibrium" was emerging and whether the Deutsche mark should be revalued to maintain the stability of the domestic value of the currency, or controlled inflation should be allowed to balance external payments. Placing a priority on stabilizing the domestic value of the currency and protecting it from the influences of external economies, Erhard and Emminger started to argue for a revaluation of the Deutsche mark in the mid 1950s. Even though there were opinions in the IMF Executive Board which called for Germany's expansionary monetary policy, Germany resisted the idea of allowing controlled inflation. Although the Deutsche mark was revalued, the change in the exchange rate itself would trigger great instability. The exchange rate issues for Germany did not come to an end with the revaluation of the Deutsche mark. Since the mid 1950s, the possibility of floating exchange rates and introducing a flexible exchange rate regime had been examined along with the revaluation of the Deutsche mark, and the discussion became more serious after the mid 1960s because of the increased scale of capital movement. Such conditions would potentially escalate foreign influences on the domestic economy, tensions emerged in the IMF system, and the intensity of the discussion regarding the ideal exchange rate system thus increased.

The main focus of Germany's monetary policy was on limiting the inflationary effects of currency inflows to a minimal level. Currency inflows from European nations emerged in 1956-57; inflows from the U. S. started after 1960. The U. S. started to recognize Germany's surpluses as a threat to its position. Such conditions coincided with judgments by IMF Managing Director, Jacobsson, and Germany was requested to export capital as "Richesse Oblige." The operation of the IMF got into gear in the mid 1950s, and Jacobsson's intentions had a considerable impact on Germany's exchange rate policies. Emminger, opposed to the expansionary policy suggested by Jacobsson, proposed to float exchange rates, criticizing the incapability of the IMF in adjusting exchange rates of its member countries.

As discussed above, Germany's capital exports were promoted starting in the second half of the 1950s. Backed by enormous foreign reserves, it provided short- and medium-term liquidity to other nations. Germany also released 18 percent of its capital to the International Bank for Reconstruction and Development (IBRD) and also provided lendings totaling 1.32 billion Deutsche marks during the 1956-58 period.[75] Our future research agenda includes the relationship between the IBRD and Germany which became a provider of liquidity after its integration into the international monetary system.

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Notes

1 The currency issues discussed in this paper are based on two articles by the author Ayako Ishizaka [Ayako Ishizaka, Discussions on the Currency Convertibility of the Deutsche Mark: 1952-1955 -in relation to "Germany's Comeback to the World Market" [Maruku no Tuuka Koukansei wo meguru Giron (1952-1955), "Doitsu no Sekaishijō e no fukki" tono Kanrenn ni oite], in: *Bulletin of Aichi Shukutoku University -Faculty of Business-*, No. 4 (2008), pp. 35-54; Ayako Ishizaka, Disequilibrium between National and International Economic Accounts in the 1950s West Germany: Dilemma of the "Social Market Economy" [1950nendai Nishidoitsu ni okeru Naigai Keizai Fukinkō, Shakaiteki Shijō Keizai no Jirenma], in: Yasuo Gonjo (ed.), *Neo-Liberalism and the Post-War Capitalism: the European and American Experiences from Historical Perspectives*

[*Shinjiyūsyugi to Sengoshihonsyugi,Ōbei ni Okeru Rekishiteki Keiken*], Tokyo 2006, pp. 255-299]; however, these issues are reexamined from new viewpoint, that is, the relationship between Germany as a creditor country and the IMF.

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