The main disadvantages of the key currency system are that it provides a particular inhibition to the policies of the countries whose currencies are so used, because the risks of speculative withdrawals of funds are so great, that the system is weakest precisely at the times when it needs most strength, namely when one of these major countries is in payments difficulties.

This happens because, at such time, confidence in one or other key currency is reduced, and there is a flight either into the other or into gold. A good deal could be done to reduce these difficulties, if the United States and the United Kingdom were, preferably jointly, to offer a gold guarantee on foreign balances held with them, to reduce the risk of speculative movements of funds.

Beyond this, there is a pressing need for a further creation of international currency. The strongest evidence in favor of this need is the fact that very few countries ever act in a way that suggests that they regard their reserves as excessive, so following the rules for surplus countries under the gold standard, while many countries act in a way which is dictated by what they regard as the inadequacy of their reserves.

Most of the burden of the deficit is thereby thrown on the deficit countries. In simple terms, there is just not enough internationally acceptable money to go around. As a result, a deflationary bias is introduced into the world economy, as by the restrictive domestic policies in Britain and the danger that expansionary policies will not be followed in the United States.

This is happening now, at a time when the world payments system is in a sense nearer to equilibrium than at any time since the war—there are now almost no large-scale surplus or deficit countries. The danger is that the equilibrium will be at an unnecessarily low level. All of which is reinforced by the tendency for an increasing amount of gold to disappear into private hoards, so reducing the available supply of international currency at a time when the need is for an increase.

The right answer is then to create an international reserve currency in adequate quantities. Many proposals have been made along these lines. In an attenuated form, they were to be found in the revision of the IMF in September 1961, but the improvements then made are already proving quite inadequate.

In the absence of an adequate and effective plan along such lines, in place of the present tendency for policies to drift toward a more rigid gold standard orthodoxy, the dilemma for American policy will in time become even more acute..

On the other hand, the United States may find itself sliding farther down the path which has been followed by Britain—that of repeatedly following policies of deflation in order to maintain the strength and prestige of sterling at a fixed exchange rate, with the long-run effect of holding back our economic progress and allowing ourselves to be overtaken industrially by rivals with no better natural resources than we possess.

On the other hand, the United States might find itself with no sensible alternative to causing unnecessary restraint on the growth of the economics of the Western World, than raising the price of gold and thereby increasing the supply of international currency.