accounts against each other daily, or even within a national economy where economic forces are allowed to operate freely. One never hears, for example, of a balance-of-payments deficit of an individual State of the United States with respect to other States of the Union. Even areas within a country that are beset by economic difficulties, such as parts of the Appalachian region, do not attempt to solve their economic problems by insulating themselves against trade with other areas of the country.

Equilibrium Without Gold

If countries allowed their domestic economies to adjust to each other by resisting the temptation to interfere with the international movement of goods and capital and by not using subsidies to interfere with internal economic adjustments, there would be continuing equilibrium among them even without the use of any gold.

Countries, however, refuse to allow their economies to adjust to each other because they have learned how to use domestic monetary and fiscal policies to stimulate economic growth and domestic employment. In consequence, with currencies pegged at fixed ratios relative to each other, and with all sorts of obstacles being placed in the way of the international movement of goods and capital, it becomes exceedingly difficult to keep the international accounts of all countries in balance with each other. Because of this difficulty, and because the achievement of balance under such circumstances requires considerable time, there is strong and continuing demand for "increased liquidity" on the part of countries that are in deficit in the form of demands for easy access to additional monetary reserves.

The question of adequacy of reserves is intimately related to the degree to which countries allow their economies to adjust to each other through changes in capital flows, merchandise trade, prices, interest rates, and wages. The greater the resistance to international adjustment, the greater will be the need for monetary reserves. Conversely, the greater the willingness to allow international adjustment to occur, the less will be the need for reserves. Indeed, "adequacy of reserves" may be conceived of as a spectrum, ranging from a need for zero reserves at one extreme to a need for almost infinite reserves at the other, the quantity of reserves needed at any time depending upon the degree to which countries resist international economic adjustments. Attempts to determine the amount of reserves needed, without reference to international adjustments, are futile.

The problem of monetary reserves is the problem of providing a deep enough financial cushion to provide time during which national economies can adjust to each other. Monetary reserves are the shock absorbers of international finance; they are not an elixir that can suddenly bring prosperity to countries that have not yet learned how to support themselves.

If foreign exchange rates were allowed to fluctuate freely no deficit in the balance of payments could occur because changes in rates of exchange would clear the market. Changes in the conditions of demand and supply in foreign trade would be met by adjustments in capital flows and in the volume and composition of international trade. Short-term capital moves internationally in response to small changes in