

organized against the dollar; there are certainly enough latent conflicts in the rest of the world to exploit *divide et impera*. But pouring oil on troubled waters is not the American way; there is surely too much of that in other parts of the world. Surely there is a better way. Both the policy of do-nothing and *divide et impera* would be abrupt changes from the historical positive role that the U.S. has played in international co-operation since the war.

There is, of course, another possibility: flexible exchange rates. After all, why not use the price mechanism to ensure balance between the supply and demand of each currency? Theoretically, such a policy is not, of course, optimal because an efficient system of payments is furthered by a single money as a medium of exchange and unit of contract. This is why, within most countries, the liabilities of one bank are convertible at a fixed price into legal tender. Indeed, if we follow Sir John Hicks' idea that each individual ought to be analyzed as a bank,¹² the idea of flexible exchange rates would be carried to its *reductio ad absurdum* since it would mean S-1 exchange rates, where S is the world's population! Of course, it is silly to carry logic that far. We live in a rather inefficient world, and as a practical approach under some circumstances, a flexible exchange rate may not only work, but be the only alternative to comprehensive controls. It is not hard to understand Friedman, Meade, and Lutz, living in a world of noxious controls and advocating, back in the 1950's, a regime of flexible exchange rates. But the world of the late 1960's is completely different: and we have a right to expect higher standards. In our present world, a system of national currencies fluctuating in terms of one another would tend to break down into a world of optimum currency areas.¹³ My own view is that we need fewer, rather than more, currencies, even though we may need more, rather than fewer, currency areas. Currency blocs have to be large if they are to make any sense at all.¹⁴ But even though some countries may want to let their exchange rates float (and there are circumstances under which they should want to), we still need an international currency for those countries who choose to remain in the international system.

This brings us back to co-operative solutions involving a common international money. With a dollar standard ruled out, and leaving aside a multiple-currency flexible exchange rate system, we are reduced to going back to gold or finding a new international currency. Going back to gold has serious disadvantages. There is insufficient gold to go around in the world at its current price, and to base a world solution on gold would mean increasing its price substantially. I have elsewhere gone into my detailed reasons for opposing an increase in the price of gold.¹⁵ I would not oppose it if there were no better alternatives. But I believe my present plan is a far better solution. But even if it were feasible or efficient to raise the price of gold, some institutions would have to be created to handle the problem of sporadic shifts in technology, discovery, and Russian gold policy, and volatile shifts between foreign exchange assets, gold, and Special Drawing Rights.¹⁶ But if an increase in the price of gold is ruled out, we are reduced to the need for a new currency. What about Special Drawing Rights?

Special Drawing Rights at the IMF have been looked upon as a form of world money. The new SDRs represent the hopes of those who believe that the world already has a new international money. But SDR units are not really money: their value is linked to gold. Even if they were true money, they have several disadvantages as an international money. I shall be going into this question in more detail elsewhere. Let it suffice for me to say that there are sins of omission

¹² J. R. Hicks, "A Suggestion for Simplifying the Theory of Money," *Economica* (February, 1935).

¹³ Some suggestions are included in my "A Theory of Optimum Currency Areas," *AER* (September, 1960), reprinted in *International Economics* (Macmillan, 1968), Chapter 12; R. McKinnon, "Optimum Currency Areas," *AER* (September, 1963); and P. Kenen, "Optimum Currency Areas, An Eclectic Approach," Chapter 2 in Mundell and Swoboda (ed.), *Monetary Problems of the International Economy* (University of Chicago Press, forthcoming).

¹⁴ I am aware that this does not dispose of the many arguments in favor of flexible exchange rates, but I do not have time to go into that question now (I intend to treat it in detail at a later date). Let me just assert that the arguments for flexible exchange rates have not progressed much beyond the primitive state in which they were put by Friedman, Meade, and Lutz. The arguments opposing them, as exemplified by the IMF *Annual Reports* of 1951 and 1962, and the Board of Governors of the Federal Reserve System in 1962, are at an even lower intellectual state, and are hardly worth discussing. The reason for the primitive state of the case on both sides is the polemical nature in which the subject has been treated, and the unfortunate tendency of protagonists on both sides to argue for victory, rather than truth.

¹⁵ "Should the U.S. Devalue the Dollar?" (Paper presented to the Western Economic Association Meetings, August 21, 1968, in Corvallis, Oregon, mimeo).

¹⁶ For example, Robert Triffin's Gold Conversion Account.