But the central bankers are today too nervous to follow such a bold policy, and I am extremely doubtful they would do so; they have not yet lost their hunger for gold. At least they would not do so outside of an organization, with wide participation. There is also the legal difficulty that the I.M.F. is required to buy gold offered to it at the current price.

The third method is to raise the official price of gold. Provided it was a substantial increase, so that speculation about a future increase is ruled out for some time, gold would flow out of hoards and we would reestablish the gold exchange standard. Reserves would be centralized in the U.S. to an increasing extent and the system would become similar to that which developed in the 1950's. How long it would last would depend on how high the price was raised. My own judgment is that if the price of gold were doubled the system might last for perhaps 15 years after which troubles similar to those experienced in the 1960's would reassert themselves.

DEFECTS OF THIS SOLUTION

The solution to halve the par value of all currencies (double the price of gold in terms of all currencies) cannot be rejected out of hand as a senseless solution to current problems. To solve problems of the system for fifteen years is not unattractive because it gives the monetary authorities fifteen more years in which to design a modern system. It, is indeed, the arrangement foreseen at Bretton Woods and embodied in the I.M.F. Articles of Agreement. Despite some attractive features, it has serious drawbacks:

1. Expectation of a second increase later on confers on gold a rate of return competitive with time deposits or other short term assets. Unless this expectation were dispelled there would be a stock shift in the demand for gold (equal to the product of the interest rate implicit in the expectation of the higher price and the interest elasticity of demand for gold as a store of value). While this amount may be negligible for the first few years it would rapidly increase over time. The "gain" from the increase could well be dissipated within a few years.

For this reason alone an increase in the price of gold would be foolish unless it were associated with a resolve of the central banks to replace gold after the increase had taken place. As things presently stand, the SDR's are looked upon as a replacement for gold. The question then is whether these will become important enough in time to convince the market that the price of gold will not have to be raised again in the future.

Given success of the SDR's this argument against an increase in the price of gold falls to the ground. But the need for an increase has to rest also on the argument that there are no better ways of achieving the same objective.

2. A second objection to an increase in the price of gold is that it is potentially inflationary. It doubles the currency value of the gold component of reserves. Now a curious argument has got about that doubling the price of gold is *not* inflationary because central banks do not have to use these reserves. The logic of the argument is extremely weak. Unless central banks are very short of reserves today they will not hold a much larger amount; if central banks were not responsive to reserve holdings most of the argument for and against increasing liquidity would fall to the ground. What has the whole liquidity issue been about if it has not assumed some connection between actual reserves and the incentive to use these reserves?

Now, of course, central banks can write the new value of reserves down on their books in whatever form they want; and they can neutralize them in various ways. But will they? Will the Bundesbank act the same way with $12 billion of reserves as with $7 billion? Will Holland with $4 billion as with $2 billion. Will the U.S. with $24 billion? I very much doubt it.

But I will grant, temporarily, for the sake of argument, what I consider to be absurd: that they would be willing to hold them. Even then an increase in the price of gold is inflationary; South African exports double in price, so that even if other prices stayed constant, some prices would rise in some countries.[5] At least the theory is clear. An increase in the price of gold is inflationary both because it increases world reserves and because it raises the value of South African exports.

The argument for raising the price of gold must then evaluate the need for an inflationary policy. In a state of world depression it would make sense. If the world moved into a state of serious depression an increase in the price of gold

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[5] Of course South Africa could appreciate the Rand, or impose deflationary export taxes.