

In the article published this month by the Banca del Lavoro I am trying to show that the President's program for correcting our payments deficit is for the birds. It is absolutely useless, or worse than useless.

I am also trying to make clear that practically all other balance-of-payments programs that have been discussed will not achieve their purpose, and that the only policy that would achieve the purpose, deflation, would be intolerable. We must not take the deflationary route to adjustment of the balance of payments. Hence, I submit that a plan that includes a widening of the present band for exchange-rate deviations from parity would do a very important service to the whole world—not just to Germany, which could avoid some inflation, not just to France, which could avoid some deflation, not just to the United States, which could avoid some embarrassment, but to the whole world, which at last would get an adjustment mechanism that can work tolerably well.

Mr. Chairman, I apologize for having taken more time than I had expected to take.

Chairman REUSS. Thank you, Mr. Machlup.

(The following letter and accompanying statement are included in the record at the request of Chairman Reuss:)

[The following statement, inserted at the suggestion of Professor Machlup, was reproduced in the New York Times with the by-line of Edwin Dale, under the date of Feb. 21, 1966]

FEBRUARY 1966.

The discussion of possible reform of the present system of international payments has been largely focused on the problem of "international liquidity." More specifically expressed, the discussion has been focused on the temporary financing of imbalances through providing additional reserves and borrowing facilities and on promoting the adjustment process through monetary and fiscal policies. The no less important issue of exchange rates has received little attention in official circles. The fact that, as the present statement shows, many professional economists can agree on a minimum program in that respect, would seem to demonstrate that there is a promising opportunity here for improving the international payments system.

Whatever the system of reserves, we believe that more exchange-rate flexibility is needed than exists under the IMF rules now in effect. It has proved impossible, under the present rules, for many countries to maintain stable prices and high employment levels and at the same time to avoid the imposition of more and more controls on international payments. To achieve these domestic economic goals simultaneously with equilibrium in external payments requires more leeway for variations in exchange rates than exists now. This is why we favor two modifications in the IMF rules.

Our first proposal is to widen the limits within which countries are obliged to keep the gold value of their currencies. This value should be allowed to vary up to four or five percent on either side of parity, instead of the present one percent. A spread of eight or ten percent would thus be provided between the upper and the lower support points. This first reform would render possible day-to-day fluctuations in exchange rates sufficient to absorb many balance-of-payments disturbances without disrupting foreign trade and investment. The proposed system need not be applied to every country without exception; some could be permitted to peg their currency to another country, or groups of countries could agree to keep the currencies of members of the group fixed in relation to one another.

The second modification we advocate is to allow countries unilaterally to change the par value of their currencies by no more than one or two percent of the previous year's par value. This seems at first more restrictive than present rules, which allow changes up to ten percent without prior approval by the IMF; yet since the present permissible changes are based not on last year's but on the originally announced par values which in many cases are now hopelessly out-of-date, our proposal is, in effect more permissive.