Bretton Woods

Even by the rarefied standards of wealthy New Englanders, the Mount Washington Hotel at Bretton Woods, New Hampshire, is a luxurious retreat. Built in 1902 by 250 skilled artisans for the then-princely sum of $1.7 million, the sprawling Spanish Renaissance-style resort, nestled in the shadow of Mount Washington, the northeast’s highest peak, has long been a favorite of celebrities and presidents. But even the man who built it, industrialist Joseph Stickney, could not have foreseen the role his creation would one day play in reshaping world history.

On July 1, 1944, delegations from 44 countries gathered from across the globe at the Mount Washington Hotel to convene what was formally styled the United Nations Monetary and Financial Conference, but which would be remembered popularly as Bretton Woods. The fruit of the labors of two men in particular, American Assistant Treasury Secretary Harry Dexter White and British economist John Maynard Keynes, the Bretton Woods conference, as much as any of the events in that momentous year, was to lay the foundation for a new international order after the Second World War, one that persists to this day.

The Bretton Woods conference attracted less interest than might have otherwise been the case, given the tenor of the times. The momentous Battle of Normandy had taken place less than a month earlier, while on the eastern front, the Red Army was poised to wrest Minsk from the Germans. In Southeast Asia, the Battle of Imphal was raging, and in American sports, a black athlete named Jackie Robinson, later to become a baseball star, was arrested on July 6 and later court-martialed for refusing to sit at the back of an army bus.

The Players

Against such a backdrop, the Bretton Woods gathering, with its focus on arid, little-understood economic and financial topics, was of little interest to much of the American public. Those journalists assigned to cover the conference found the participants less than forthcoming about much of what went on behind closed doors in the Mount Washington Hotel.

For those in the know, however, the event was one of the most significant gatherings of international power elites the world had ever seen. Heading the American delegation was Secretary of the Treasury Henry Morgenthau, although he played a less significant role in the conference than his assistant, economic wunderkind Harry Dexter White. It had been White who, following a teaching stint at Lawrence University in central Wisconsin, had come to Washington in the mid-1930s and ended up in charge of the Treasury’s Division of Economic Research. As a result of working to set up an Inter-American Bank to stabilize currency values, White had conceived of an idea for a global entity to regulate monetary values and protect individual currencies from failing.

Also prominent in the American delegation was Assistant Secretary of State Dean Acheson. Later to become Truman's Secretary of State, Acheson was involved in the creation of the United Nations and the Marshall Plan, and is regarded as the man most responsible for persuading President Truman to intervene in the Korean War. He also became known in some circles as something of a communist sympathizer: he was blamed for encouraging the Maoist takeover of China, and he expended a great deal of energy defending accused communist spy Alger Hiss and many communists and communist sympathizers fingered by Senator Joseph McCarthy.

Mariner Eccles, former Utah banker-turned-chairman of the Federal Reserve, was also part of the American delegation, as was Fred Vinson, one time-congressman and then-Director of the Office of Economic Stabilization, who later became President Truman's Treasury Secretary.

Heading the British delegation was John Maynard Keynes, the eminence grise of British economics and the only economist (if Karl Marx is excepted) whose surname is affixed to a major system of economic thought. Brilliant but abrasive, Keynes had been arguing for years for some kind of international economic and financial system to replace the havoc allegedly wrought by cut-throat capitalism in the international currency markets and balances of trade. Keynes wanted to set up a global financial authority that would issue an international currency in which all other currencies would be reckoned. Keynes proposed naming the new currency the bancor; the Americans supported the idea, but preferred calling it the unitas.

Other delegations brought proposals of their own, or came with special concerns. The Soviet Union, for example, was a major producer of gold and wanted to ensure that this industry would continue to give them leverage in any new international system.

While there were differences in opinion and even sharp conflicts of interest, all assembled at Bretton Woods in July 1944 were agreed on three things: first, that something had to be done to deal with international financial instability; second, that that something would entail setting up some kind of global authority, a financial and economic counterpart to the League of Nations and its soon-to-be-birthed successor, the United Nations; and third, that White and Keynes were to be the undisputed leaders of the conference proceedings.

Not unexpectedly, the conference was fraught with personal and political issues from the get-go. The French delegation, representing the Algerian French government in exile, proved particularly sensitive to what its delegates perceived as slights to French interests and disdain for their lack of independence. The Russians used their gold reserves as a bargaining chip to obtain multiple concessions with regards to their stipulated contribution to the International Monetary Fund. And the British were suspicious of American nationalism and desire for privileged economic status, which, Keynes later reported in a letter to Sir John Anderson, British Chancellor of the Exchequer, made them "intolerably tiresome in method and in detail and with the execution of plans and in the mode of pressure they bring to bear…. They have their own difficult psychology and a dreadful tendency to suspicion and all the rest of it." The American-British rivalry took a personal turn when Henry Morgenthau lost a critical night's sleep thanks to Lady Keynes, an accomplished ballerina who, lodged in the room directly above the American Treasury secretary, practiced her dancing at all hours of the night.

Behind all the pomp and personality clashes, the issues at stake at Bretton Woods were of critical importance. Although personal ideologies differed in degree among the delegates (Harry Dexter White, for example, was later accused by the FBI of being a communist agent, whereas Henry Morgenthau claimed to be a "conservative" who detested the new Keynesian economics), all were in basic agreement that an international overhaul of the world's financial and economic system was in order, and that any such overhaul needed to be accomplished by government controls, both nationally and internationally.

Bretton Woods, in other words, was an undertaking hostile both to free-market capitalism and to economic self-determination; it sought unblushingly to create a world financial and economic order — to lay the foundation for a global command economy — at the same time that a new international political order, the United Nations, was being planned. (The famous Dumbarton Oaks conference, a much more exclusive and secretive gathering in which the United Nations Charter was drafted, took place the month after Bretton Woods.) The animating philosophy behind Bretton Woods, which has since become the predominant economic doctrine the world over, was so-called Keynesian economics, the philosophy that attempts to repudiate free-market economics and replace it with interventionism.

The Backdrop

By the time of Bretton Woods, the schools of economic thought, chiefly French and British, that had held up free-market capitalism as the highest ideal, had largely been supplanted in the so-called mainstream by various strains of interventionist dogma, ranging from the ranting extremes of Marxism to the milder but no less socialistic musings of Keynes, Thorstein Veblen, and other prominent economists hostile to the free market. (Champions of free-market economics, like Ludwig von Mises and his most eminent student, future Nobel Laureate Friedrich Hayek, existed, but few at the time were interested in their ideas.) The free market has always been something of an ideal, given the messy reality of taxes, tariffs, and the like, but the 19th century saw laissez-faire principles practiced more consistently in the United States, in the British Empire, and elsewhere in the West, than has ever been the case since. Taxes were low, tariffs and international trade barriers were lifted, and capital formation was encouraged, thanks in no small measure to the writings of free-market economists like Adam Smith and Jean Baptiste Say, who did for economic freedom what John Locke and Thomas Jefferson did for political freedom.

But the rise of Marxism and other strains of big-government radicalism (like St. Simonism and, in the United States, the misnamed "Progressive" movement) put an end to all that. By the early 20th century, the brief, glorious period of limited government, in the United States and in Europe, had come to an end. The old fallacy of government as universal overseer had reasserted itself, and self-styled visionaries sought to enlist the power of the state to right every wrong, real or perceived. Laws to rein in the alleged excesses of the free market, from long working hours to low wages to the formation of so-called monopolies, appeared in the United States and abroad, and innovative new forms of taxation, most prominently the progressive income taxes recommended by Karl Marx in his *Communist Manifesto*, confiscated private wealth ever more aggressively.

At the same time, political leaders longed for ways to raise unlimited revenue to fund their Utopian schemes. Clearly, direct taxation had political limitations, since hard-pressed citizens and subjects would not endure confiscatory taxes indefinitely. For the modern state to achieve its true potential, it was widely believed, some other open-ended means of raising revenue besides taxation was necessary, something that would emancipate politicians from the limits of mere taxation.

This something was central banking, specifically, the issuance of unbacked paper (or "fiat") money, whereby governments could effectively print the money they needed to fund wars, welfare programs of every description, and other grand spending projects that even a heavy progressive income tax could not adequately fund.

Fiat money had been tried sporadically before — in the Massachusetts Bay Colony, during the American Revolutionary and Civil Wars, in the run-up leading to the infamous South Sea Bubble, and in Napoleonic Vienna, for example — but always locally and always with calamitous results. Long experience showed that people preferred gold and silver ("specie"), or "bills of credit" reliably backed by the same, to pieces of paper whose value depended solely on the say-so of government. Paper money always proved ruinous in the long run because men could not be trusted to limit its issue. As James Madison once presciently observed:

> It cannot be doubted that a paper currency rigidly limited in its quantity to purposes absolutely necessary, may be made equal and even superior in value to specie. But experience does not favor a reliance on such experiments. Whenever the paper has not been convertible into specie, and its quantity has depended on the policy of the government, a depreciation has been produced by an undue increase, or an apprehension of it.

A pure fiat money system remained a pipe dream of crank economists and wistful international bankers and financiers, all of whom hated what Keynes, in a press conference during the Bretton Woods conference, disparagingly called the "tyrannical powers" of gold. Gold, by virtue of its limited supply, divisibility, portability, durability, and other factors, was not only the ideal medium of exchange but also tended to hold government spending in check, since no politician possessed a magic wand to produce it in unlimited quantities. Keynes obviously wanted a magic wand to print fiat money, and he saw gold's denial of that wand as being tyrannical.

Any government that tried to inflate its currency relative to its gold holdings promptly saw that currency depreciate and its gold reserves move abroad. In a world of specie-based currencies, no international regulatory bodies were necessary because all currencies were simply different names for quantities of gold.

World War I changed all that. The first great international war in three centuries provided the long-awaited pretext for governments to go off the gold standard en masse. The great central banks of Europe began to print vast amounts of money to fund the war effort, producing massive inflation (and, in the case of postwar Germany, hyperinflation that completely destroyed the value of the German mark). The United States remained nominally on the gold standard but, with the creation of the Federal Reserve in 1913, a modern central bank patterned after the European model, also acquired the ability to finance projects like wars by deficit (i.e., inflationary) spending.

The wartime inflation led to a brief but sharp postwar recession in the United States and elsewhere. During the 1920s, Great Britain, terrified of having to face depreciation of the pound as a result of running the printing presses, pressured the United States and other powers to inflate in concert with the Bank of England, leading to another global inflationary cycle and economic bubble that burst in 1929 with the great stock market crash. A few years later, during the Great Depression, the United States effectively followed the nations of Europe in abandoning the gold standard. While the dollar remained convertible to gold for foreign investors, privately held gold was confiscated, legal tender laws were enacted requiring American citizens to accept government paper as money, and private ownership of gold bullion was prohibited.

But the abandonment of gold led to international financial volatility, as individual governments, freed from the stabilizing restraints of gold, inflated or contracted their money supplies at will. Currency crises of the type so familiar in our own day became commonplace, with exchange rates difficult to anticipate in a world where national money supplies were constantly changing by dramatic amounts.

Task at Hand

In such a world, men like Harry Dexter White and John Maynard Keynes — special pleaders on behalf of powerful political and financial interests who had always inhabited the fringes of economics — suddenly became relevant, even though their line of thinking turned classical economic thought (not to mention common sense) on its head. From Keynesian advocacy of fiat money over gold flowed an entire cluster of fallacies made necessary to defend the indefensible. Because fiat money always depreciates over time, and because its issuance depends crucially on the willingness of the public to incur debt (new money is typically created by issuing unbacked debt which then enters the money supply when spent), savings, the old concomitant of thrift, was disparaged. In the Keynesian view, because fiat money created by and manipulated by the state is superior to gold ("that barbarous relic," Keynes called it), economic growth depends not on the accumulation of wealth via savings but on spending and consumption.

Keynes, who had undoubted persuasive gifts, found in 1930s America and Great Britain more pliant audiences for his radical ideas than would have been the case a few decades earlier. It was Keynes that economist and journalist Henry Hazlitt had in mind when he wrote, in the mid-1940s:

> There are men regarded today as brilliant economists, who deprecate saving and recommend squandering on a national scale as the way of economic salvation; and when anyone points to what the consequences of these policies will be in the long run, they reply flippantly, as might the prodigal son of a warning father: "In the long run we are all dead." And such shallow wisecracks pass as devastating epigrams and the ripest wisdom.

Thus the task at Bretton Woods was to provide a government remedy for problems that government had created in the first place — currency instability and international recession brought about by the abandonment of the gold standard. The agenda items, drawn up at a conference in Atlantic City a few weeks earlier, included the creation of a global currency, an international monetary fund to which all member countries would subscribe by surrendering a certain amount of their gold reserves, a global body to regulate trade, and an international bank to provide loans to needy countries for development.

In the International Monetary Fund, Keynes and White got most of what they wanted, except that no new global currency was set up. Instead, the signatories agreed that their currencies would be pegged to gold or (in a piece of verbal sleight of hand that many signatories to the agreement apparently overlooked) to the U.S. dollar. For the time being, then, the dollar remained convertible to gold internationally; even Bretton Woods had not completely overcome the "tyranny" of gold. (That was to come to pass three decades later, when the Nixon administration "closed the gold window," abandoning the dollar's convertibility to gold and setting the stage for 30 years of wild inflation that followed.) The International Bank for Reconstruction and Development, the first iteration of what became the UN's World Bank Group, was also birthed amid great fanfare. Less successful was the first attempt to create what was then called the International Trade Organization (ITO). The most that Bretton Woods could achieve for trade was a draft for what came to be called the General Agreement on Tariffs and Trade (GATT), along with a commitment to periodically renegotiate the agreement until the hoped-for global trade authority could be put together. Fifty years after Bretton Woods, the World Trade Organization (WTO) became reality, and the GATT agreement was formally superseded.

Specter of Bretton Woods

On the final night of the Bretton Woods conference, John Maynard Keynes was honored at a black-tie dinner. Looking wan and exhausted (Keynes had suffered a heart attack during the conference, a precursor to another that would take his life in 1946), Keynes addressed the august gathering in a spirit of smug triumphalism:

> We, the delegates of this Conference … have been trying to accomplish something very difficult to accomplish…. We have had to perform at one and the same time the tasks appropriate to the economist, to the financier, to the politician, to the journalist, to the propagandist, to the lawyer, to the statesman — even, I think, to the prophet and to the soothsayer…. We have reached this evening a decisive point. But it is only a beginning. We have to go from here as missionaries, inspired by zeal and faith. We have sold all this to ourselves. But the world at large still needs to be persuaded…. We have perhaps accomplished here in Bretton Woods something more significant than what is embodied in this Final Act. We have shown that a concourse of 44 nations are actually able to work together at a constructive task in amity and unbroken concord. Few believed it possible. If we can continue in a larger task as we have begun in this limited task, there is hope for the world…. If we can so continue, this nightmare, in which most of us here present have spent too much of our lives, will be over. The brotherhood of man will have become more than a phrase.

Keynes sat down from the culminating event in his career to thunderous applause and a chorus of "For He’s a Jolly Good Fellow." For Harry Dexter White, on whom Keynes lavished effusive praise, Bretton Woods was also the beginning of the end. In early 1946, shortly after being appointed by President Truman as director of the IMF, the FBI produced damning evidence that White, since the late 1930s, had been involved in high-level communist espionage, bringing members of the communist underground into the Treasury Department and passing information to Soviet spies. White was relieved of his government responsibilities and, in 1948, shortly after denying his communist activities to the House Un-American Activities Committee, died of a heart attack.

The specter of Bretton Woods still haunts international finance and global trade. The IMF, WTO, and World Bank continue to hamper international free markets and crimp the sovereignty of nations. The current global economic and financial crisis, created by precisely the policies that Keynes and his epigones have promoted for decades, has prompted calls for a "Second Bretton Woods." The recent world economic summit in Washington has already been billed as the start of a process that will take care of unfinished business left over from the first Bretton Woods. British Prime Minister Gordon Brown predicted, in a speech before the New York-based Council on Foreign Relations on the eve of the conference, that the new round of negotiations would produce an IMF that "looks more like a global central bank" — exactly what the shades of Keynes and White would wish, we need hardly add.

Keynes was, like most prominent men, a patient visionary. As his concluding speech implied, he saw Bretton Woods not as an endpoint but as the beginning of a long and arduous process that would someday culminate in the reality of a "brotherhood of man" – code for "a single world state." Unless vigilant Americans can halt the momentum toward a global currency, a global central bank, a global financial regulatory ministry, and other long-held conceits of the "one worlders," Keynes’ vision — the real goal of Bretton Woods — is likely to become reality sooner rather than later.