Jacques de Larosière

The topicality of Robert Triffin

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Mr. Governor, Ladies and Gentlemen,

It is with great pleasure that I participate in the presentation of my friend Ivo Maes' remarkable book on Robert Triffin.

It is an important book, and I will highlight its topicality. It should inspire us all.

I – What are the "anomalies" of our international "system" such as Robert Triffin denounced them 60 years ago?

1. The richest country in the world, the United States, lives on credit and thrives on being financed by others, even the poorest.

2. The players in the system are free to choose their exchange rate policy: sometimes they let it float, or they "manage" it avoiding appreciation in order to maintain the desired competitiveness (notably by buying dollars).

3. The effort to adjust balance of payments imbalances falls exclusively on deficit countries (with the exception of the United States) and not on countries with structural surpluses.

4. Supplying the world with liquidity is mainly due to the external deficit of the United States. (Creditors buy dollars).

One of the problems with these "anomalies" is that you get used to them and don't try to make things better anymore.

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II – The « dilemmna ».

Triffin has done a great deal to analyse these deficiencies and try to remedy them.

He was one of the first to understand the contradiction inherent in the "Bretton Woods system", designed at the end of the war to restore a world economic and monetary order.

For about 15 years, the system set up around the International Monetary Fund in 1944 has worked fairly well: The United States combined a balanced current-account balance and capital outflows that irrigated the world in search of dollars. And the deficit countries - impoverished or destroyed by war - benefited from capital inflows and relative macroeconomic discipline.

But this system got out of hand at the end of the 1960s and it was to Robert Triffin's credit that he was one of the first to understand it and to demonstrate it with a remarkable independence of mind, lucidity and foresight.

The rise in public expenditure in the United States was the cause of this disruption.

Indeed, it was necessary to finance the Welfare State that developed in the USA after the war, then the Vietnam War, which was a real abyss in terms of public spending.

Rather than finance these waves of spending through taxes – or savings –, the United States resorted to borrowing. The world - still looking for dollars to ensure its growth – thus financed the growing deficit of the United States by buying, with its savings, the debt issued by the Americans.

But in doing so, the ratio of US dollar debt to the US gold stock deteriorated. However, the “Bretton Woods system” was based on the gold convertibility of dollars held by foreign central banks.

Triffin was the one who formulated the famous “dilemma”:

- or the United States control their budget and current account balances by restricting domestic consumption and the world runs the risk of a recession;
- or they finance on credit their development as well as the Vietnam War and the abundance of dollars thus created will one day show the impossibility to ensure the convertibility of the dollar into gold.

It was the second branch of this alternative that came about and, on 15 August 1971, the United States put an end to the gold convertibility of the dollar. The international monetary system gave up - 30 years after instituting it - the system of fixed exchange rates.

III – The current “non-system” and the need to correct it.

But the end of Bretton Woods was not going to solve the problems.

For a time, it was thought that abandoning fixed exchange rates would solve everything:

With flexible rates, it was thought that States – and first and foremost the United States - were going to recoup freedom to choose their policy mix: imbalances would naturally be resolved by exchange rate fluctuations on the markets and by capital movements now free from controls.

At last, the world was free !

But, in fact, the world has not “liberated”. It has become increasingly dependent on financial markets, which have, with accompanying innovations, taken the predominant place in the functioning of the international monetary system.

This “non-system” - the one where we live – is characterized by:

- Massive global indebtedness (always generating financial crises, bubbles and defaults);
- A preference for holding liquid assets rather than long-term investments (which we so badly need);
- Maintenance of the “exorbitant privilege” of the dollar: US deficits remain the central element of the supplying the world with reserves, and the US continues to live on credit;
- The extreme modesty of the attempt to create an international currency advocated by Keynes and Triffin (SDR).

Ultimately, the imperfections denounced by R. Triffin can only be resolved by moving towards greater international cooperation.

One of the lessons of the R. Triffin’s work is important to meditate on: it is the author’s interest in international “institutions”. He always believed that the IMF, and later the European institutions, should play a key role in the organisation of our system.

In this regard, I would like to recall the following episode:

When, in 1949, an orderly devaluation of the exchange rates of a large number of countries had to take place, Britain – whose other countries had been waiting for the decision before taking a position – did not want the IMF to intervene. The US Director at the IMF, Mr. Southard, therefore organized “informal” discussions at the IMF to assess reasonable amounts of future devaluations. But the British insisted that the Director General, Mr Gutt, should not participate in these discussions. Triffin - he was under 40 - vigorously denounced this attitude contrary to the IMF’s Articles of Agreement.

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In short, the following points remain highly topical and call for action.

- Any "orderly" international system cannot ignore exchange rate relations between large countries;

- It is therefore necessary to entrust an independent and competent monetary organization with the task of supervising exchange-rate relations. This does not mean a return to absolute fixed parities between major currencies. But this implies agreement on the idea of seeking a rational and desirable operational link between exchange rates and economic policy;

- This is important, especially in a context of "super leverage" like the one we know. In fact, the triggering of the economic cycle is now a matter of finance. It is the monetary policy of the United States that rules the world. Its changes make their mark on the financial cycle. It would therefore be logical to pay a little more attention to the international implications of monetary policy of large states from the point of view of financial stability.

- And economic adjustment should be at the forefront. A stable international monetary system should be based on adequate economic cooperation. Perhaps this is the weak point in Triffin's thinking. He devoted more attention to the financing of balance of payments deficits than to the necessary adjustments to be introduced.

Otherwise, there is a risk of a proliferation of exchange rate wars – by means of monetary policy – and protectionism, which always are ominous.

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