The big message of this little book is that history must be read carefully for its policy implications. I take as my foil a series of articles by Michael Dooley, David Folkerts-Landau, and Peter Garber, three authors who have influentially used the history of the Bretton Woods international monetary system that operated from the late 1950s through the early 1970s to make some points about the operation of today's international financial system. Then as now, according to Dooley, Folkerts-Landau, and Garber, the United States occupied an asymmetric position at the center of the international system, running balance-of-payments deficits, providing international reserves to other countries, and acting as export market of last resort for the rest of the world. Other countries kept their currencies pegged to the dollar. They were reluctant to revalue even in the face of chronic American balance-of-payments deficits and even where they enjoyed relatively rapid productivity growth for fear of interrupting the process of export-led growth and suffering capital
losses on their foreign reserves. The original Bretton Woods system, based on these structural factors, endured for many years. The implication is that the new informal Bretton Woods system that has developed spontaneously in recent years is likely to prove equally durable. To put it another way, since structural factors underlie the current pattern of exchange rates (undervalued Asian currencies and an overvalued dollar) and global imbalances (Asian surpluses and U.S. deficits), this situation is likely to endure for a considerable time to come.

As always, the closer one examines a history, the more complicated it appears. On closer scrutiny, important differences are apparent in the structure of today’s world economy compared to the 1960s. Taken together these factors point to the conclusion that the current constellation of exchange rates and payments imbalances is unlikely to persist for as long as the original Bretton Woods system.

A broad overview of these differences is provided in chapter 1. Subsequent chapters then develop the contrasts in more detail. Chapter 2 examines the Gold Pool, the collective agreement through which the central banks of other advanced nations attempted to resist the temptation to diversify their reserves out of dollars into gold and thus to prevent their currencies from rising. It suggests that the history of the Gold Pool is less than reassuring for those who believe that contemporary central banks will continue to act collectively to support the dollar. Chapter 3 examines the case of Japan, a country that had long pegged its currency to the American dollar and pursued a
policy of export-led growth but that revalued and then
floated in 1971 to 1973. Its history suggests that it is pos-
sible for a rapidly growing, export-dependent economy to
exit from a peg without killing the golden goose of
growth and that differences between Japan then and
China now make this potential scenario even more likely
today. Chapter 4, finally, draws out the implications of the
fact that today, unlike in the 1960s, there exists a full-
fledged rival to the dollar in the form of the euro.

Each of these chapters illustrates the power of historical
analogy in informing interpretations of current circum-
stances and future prospects. But the power of analogy
resides not just in drawing out the parallels between
two historical settings but also in highlighting the differ-
ences between them. It is those differences and their
relatively pessimistic implications for the prospects for
the dollar and the world economy that are emphasized in
this book.

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