SUBJECT

cc OPS
Master

T. JO NMKS

10 DOWNING STREET

THE PRIME MINISTER

30 March 1983

PRIME MINISTER'S
PERSONAL MESSAGE
SERIAL No. T43/83

Dear Rob.

I was interested to read your address to the European Management Forum Symposium at Davos which you kindly sent me on 4 March.

In my letter of 1 December, I described my own approach to the issues which you have rightly identified for public debate.

I would like to add one general comment to what I said then. I think you may understate the progress that the international community has made.

There are signs that the inflationary habits of the 1970s are being broken. Interest rates have come down. This will, most of us believe, provide room for greater real growth of activity. And lower oil prices should reinforce the prospect of economic recovery.

The Interim Committee meeting in Washington in February also made solid progress. The GAB and Quota decisions were judged by the Managing Director to have effectively doubled IMF resources in terms of usable currencies. The decision

/to implement

to implement those increases quickly directly responds to one concern you expressed at Davos. The new initiatives taken by the IMF to encourage commercial banks to play a continuing part in the adjustment programmes of debtor countries is relevant to another. Of course more needs to be done, and this is perhaps particularly true in the trade field, where the current problems are, I agree, inseparable from payments issues. But we have taken some real steps forward, and I think they go beyond what you have called "band aid" solutions!

Warm regards

Yours sincerely

Margaret Thatcher

The Right Honourable R.D. Muldoon, C.H., M.P.

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Indebtedness

Pt 2

RESTRICTED

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

28 March 1983

A J Coles Esq
10 Downing Street
LONDON SW1

Type letter pl.

A.J.C. 28/3.

Dear John.

MR MULDOON AGAIN

With your letter of 14 March you enclosed a further letter Mr Muldoon had sent to the Prime Minister about the case for a new Bretton Woods Conference.

Mr Muldoon enclosed this time a copy of his address to the European Management Forum Symposium at Davos. His covering letter suggests that recent pronouncements by Donald Regan, George Shultz and Helmut Schmidt indicate sympathy with the Muldoon approach.

... A summary of the Davos speech is attached. It is essentially the same as the speech Mr Muldoon gave at Suva last autumn and sent to the Prime Minister. We know from Peter Marshall that the Prime Minister last time sent a long reply - perhaps based on the draft I sent you on 29 November - and that it was greatly appreciated. But a shorter, rather cooler reply, drawing attention to the progress being made by the international community, may be appropriate this time, given that the ideas Mr Muldoon advances have hardly changed.

Part 1

... A draft on those lines is attached.

Yours ever,

John Kerr.

J O KERR

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DAVOS SYMPOSIUM: ADDRESS BY MR MULDOON

General

Need for new Bretton Woods Conference to develop a co-ordinated set of policies to govern international trade and payments. Financial dislocation and protectionism feed on each other.

Historic background

Collapse of Bretton Woods system compounded by first oil shock. Subsequent high inflation and interest rates, unemployment, volatile exchange rates. Ad hoc international response. Recycling masked inadequate adjustment. Growth of debt burden.

Payments: current indications of strain

14 reschedulings sought in 1981: 40 countries 'in trouble' in 1982. In some cases debt service exceeds total exports. Over exposure of private banks. Attempts by banks to cut back aggravates problem.

Payments: solutions

Closer liaison between commercial banks and IMF.
Doubling of IMF quotas implemented quickly.
Long term bond issue, guaranteed by international agency, to relieve position of chronic debtors.
Easier Fund conditionality.
Symmetrical Fund Surveillance.
New decision making Council.
Substitution Account.
Increased aid flows.
SDR Aid Link.

Trade: current problems

GATT founded to deal with tariffs: but
Growth of NTBs ('600 different types').
50% of trade 'managed'.
Exchange fluctuations make nonsense of tariffs.
Trade restrictions abort past investment.

Trade: solutions

Major countries now emphasising need for 'co-ordinated expansionary policies'.
New opportunity needed for developing countries to trade their way out of difficulty.
This essential also for economic welfare of industrial countries (one third of whose manufacture exports go to developing countries).

Conclusions

Need for broad-based reappraisal. Summits can agree on analysis but are deficient on action. Operations of post war institutions have unravelled tight connections between trade and payments: must be put together again.

DRAFT LETTER FROM THE PRIME MINISTER

TO: THE RT HON R D MULDOON CH

I was interested to read your address to the European Management Forum Symposium at Davos which you kindly sent me on 14 March.

In my letter of 1 December, I described my own approach to the issues which you have rightly identified for public debate.

I would like to add one general comment to what I said then. I think you may understate the progress that the international community has made.

There are signs that the inflationary habits of the 1970s are being broken. Interest rates have come down. This will, most of us believe, provide room for greater real growth of activity. And lower oil prices should reinforce the prospect of economic recovery.

The Interim Committee meeting in Washington in February also made solid progress. The GAB and Quota decisions were judged by the Managing Director to have effectively doubled IMF resources in terms of usable currencies. The decision to implement those increases quickly directly responds to one concern you expressed at Davos. The new initiatives taken by the IMF to encourage commercial banks to play a continuing part in the adjustment programmes of debtor countries is relevant to another.
Of course more needs to be done, and this is perhaps particularly true in the trade field, where the current problems are, I agree, inseparable from payments issues. But we have taken some real steps forward, and I think they go beyond what you have called "band aid" solutions!

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Pt 2

10 DOWNING STREET

From the Private Secretary 14 March 1983

International Financial Situation

With your letter of 29 November, you enclosed a draft letter for the Prime Minister to send to Mr. Muldoon in response to his letter of 22 October.

I now enclose a copy of a further letter which Mr. Muldoon has sent to the Prime Minister (and which he has also copied to the Chancellor of the Exchequer). I should be grateful if you could let me have a draft reply for signature by the Prime Minister in due course.

A.J.C.

John Kerr, Esq.,
H.M. Treasury.

SUBJECT

CC Master Ops

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PRIME MINISTER'S PERSONAL MESSAGE
SERIAL No. T25C/83

Prime Minister
Wellington
New Zealand

4 March 1983

R12

The Right Hon. Margaret Thatcher MP
Prime Minister
10 Downing Street
London SW1
ENGLAND

Dear Margaret,

Since our correspondence late last year concerning my proposals for a comprehensive examination of the trade and payments system, there has been a good deal of public debate on the question. A growing number of voices, and not just within the developing world, are now making very similar proposals. We have already seen the United States Secretary of the Treasury, Mr Regan, suggest that there was a need to lay the groundwork for an international meeting on trade and payments - only to withdraw it quickly when, as I see it, it became apparent he was rather too far in front of the consensus in the United States. I have been gratified that George Schultz seems to recognise that the improvement of the world economy is of overriding importance to US foreign policy objectives. Helmut Schmidt's recent essay in the Economist covers very similar ground to my proposals.

While remedial steps are taken to deal with immediate problems - the recent decisions on Fund quotas and the General Arrangement on Borrowing come into that category - this debate on the longer term issue of how we might build on the existing trade and payments institutions will continue. I expect it to figure very prominently in the forthcoming calendar of international economic meetings.

As part of that process of debate I am circulating to selected political leaders copies of my latest address on the subject. This was the address I gave in January to the European Management Forum symposium held each year in Davos, Switzerland. A copy is attached, for your information.

...2.

I am taking the liberty of sending a copy to your colleague, Sir Geoffrey Howe, who, as Chairman of the Interim Committee, will play a key role in these matters.

With kind regards

Yours sincerely

Address by

Right Hon. R. D. Muldoon, C. H.

Prime Minister of New Zealand

to

European Management Forum

Davos, Switzerland, 27 January 1983

The Right Hon. Robert David Muldoon was born in Auckland, New Zealand, on 25 September 1921. He entered Parliament in 1960 and was Minister of Finance from 1967 to 1973. He has been Prime Minister and Minister of Finance since 1976.

As Minister of Finance, Mr Muldoon is a Governor of the Asian Development Bank (1969–1972 and 1976 on) and Governor for New Zealand of the International Monetary Fund (1967–72 and since 1976). He was chairman of the joint boards of governors of the I.M.F. and the World Bank for the 12 months ended October 1979. He was also chairman of the 1982 OECD Council of Ministers.

Address to European Management Forum

Davos, Switzerland, 27 January 1983

When I accepted an invitation to address this symposium, the first thought that occurred to me was that my audience would be composed overwhelmingly of practical people. People who rise to the most senior positions in government, business and the major international economic institutions tend to develop a keen sense of the possible.

I was also conscious of the fact that some 50 years ago Keynes had observed that practical men believe themselves to be exempt from any guiding ideas or intellectual influences.

Here is the conundrum. The proposition I wish to put before you practical people is very much an idea. It is an idea I have developed over a period of several years but crystallised into a set of proposals over the last six months or so. Put in its simplest terms the proposition is this: the gravity of the problems we now face requires us, as a world community, to sit down, as we did at Bretton Woods in 1944, and develop a co-ordinated set of policies to govern international trade and payments for the rest of this decade and beyond. We have a clear choice: we can either begin to search now for comprehensive solutions to the problems caused by the collapse of the Bretton Woods system or wait for the situation to deteriorate further when we would be forced to do so but in much less propitious circumstances.

I am taking the unusual step of presenting my conclusion before I present my analysis. I am doing this because my experience from various Commonwealth meetings has been that few people have queried the analysis, but there is a tendency to misinterpret the conclusion. One group of countries, and within the Commonwealth context they would form the large majority, enthusiastically support the proposals—in part, I suspect, because they see them contributing to their objectives in the North-South dialogue. The other group of countries, which has fought hard to keep international financial issues off the agenda for Global Negotiations, is inclined to see any critique of the existing framework for international trade and payments as dangerous in itself. No matter that the problems are so great as to threaten to overwhelm that system. Better the devil you know would be a reasonable summation of their attitudes.

The reaction to recent comments of Donald Regan on these same issues is a case in point. You will recall that the US Treasury Secretary on 6 December reached the conclusion that there was an urgent need to go beyond the ad hoc approaches of recent years and to start thinking about a concerted approach to the interconnected problems of protectionism, disinflation and debt. He referred to the need to lay the groundwork for some type of international meeting to examine these issues whereas I have used the shorthand of 'another Bretton Woods', simply to fix the scale of the task in people's minds. Yet within a matter of days of Mr Regan's comments, the usual levelling out process had begun. Mr Regan, we were informed, was voicing his personal views. Mr Regan was not, we were assured, calling for another Bretton Woods. Mr Regan was not briefed to say this, and so on. You will of course appreciate that it always causes the utmost surprise and consternation to advisers when a Minister demonstrates he is capable of forming an independent conclusion.

What I hope you will conclude from my analysis is that in calling for changes to international financing arrangements I am not attacking the International Monetary Fund and its sister bodies. I am urging that their role be strengthened. In calling for increased aid flows I am not undermining the pre-eminent importance of sound domestic economic management. I am suggesting that there are a number of serious deficiencies in the way in which we are currently trying to patch over the twin problems of growing financial disorder and growing protectionism. I believe that if we do not find some means of tackling these issues, the economic, political and indeed strategic consequences for the West will be most serious.

It will be a matter for historians to trace the background to our current difficulties. For practical purposes we could say they began with the collapse of the Bretton Woods system in the early 1970s and were compounded by the first oil shock. For some ten years since then we have faced such things as high and differential rates of inflation, massive unemployment, excessive interest rates,

financial crises and volatile movements in exchange rates that cannot be fully explained by differences in relative costs or trading performance.

The international community has responded in a fitful and ad hoc fashion, but always with supreme, although unjustified optimism for the future. The total situation has in fact continued to deteriorate. In 1972 I was present at an inaugural meeting of the Committee of Twenty which was set up to devise new rules to put in place of the rules for international monetary co-operation that were agreed at Bretton Woods. I was then, also, an optimist. The Committee of Twenty lasted for rather less than two years at which time the first of the oil shocks hit.

The response of the Committee of Twenty was to change its name. It then became known as the Interim Committee. Since then the Interim Committee has been largely concerned with short-term policy matters affecting the IMF. I am not belittling the progress made in establishing new financing facilities but merely questioning whether this was commensurate with the scale and nature of the long term financial problems emerging in the marketplace.

In the marketplace the immediate problem was to recycle funds to the deficit countries. In some respects, the recycling process was extremely successful. Certainly it achieved its main objective of avoiding default. Until very recently, few countries found it difficult to raise from the private capital markets the vast sums required.

In too many cases, however, the very ease of raising funds has masked the adjustment process. The money was lent by the private banks with very little thought or with excessive optimism as to the capacity of the countries to pay it back. Quantity, not quality, was the hallmark of those financial operations over the last 8–10 years.

As far back as 1976 at the annual meetings of the IMF and World Bank, I was arguing that the problems of the deficit countries were growing problems that would inevitably worsen and ultimately threaten the stability of the world economy. What has been overlooked has been that each year's deficits have been added on to the accumulated deficits of all the previous years. From 1973 to 1981 the longterm debt of less developed countries grew at an annual average rate of 20 percent. The net result, of course, has been that the debt service ratios of these countries has deteriorated year by year to the point where for many of them the position is unmanageable.

Where do we stand now? The aggregate picture is disturbing enough in itself. However, the aggregated statistics do not tell the whole story. Some countries have done well, but others are much

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worse than the average. In 1981, fourteen sovereign countries sought reschedulings of their external debt, in spite of the implications of their longterm reputations as borrowers. By 1982, some forty countries were in trouble and a considerable number of countries were facing the ludricous position whereby total debt service payments—that is, interest payments plus all debt falling due in that year—exceeded their entire earnings from the export of goods and services. The better-placed deficit countries with reasonable debt service ratios—such as New Zealand—may well benefit from this because they will tend to look more attractive to lenders. Where, however, does this leave the countries in real difficulties, and those who have lent them vast sums of money?

From all this, we can deduce one salient fact: these countries are facing longterm structural balance of payments difficulties quite different from the cyclical difficulties envisaged by the founders of the International Monetary Fund. Some of them will trade their way out of this only in the very long term, if ever. All of them will require medium to longterm financing arrangements.

This is something which the existing structure of capital flows is not well equipped to handle. Consider its components: private capital flows, official capital flows at market or near market rates, and aid flows.

The private banking system as a whole is seriously over-exposed. The nine biggest banks in the United States have lent the equivalent of 40 percent of their capital and reserves to one country alone—namely Mexico. The tendency, of course, is now for the smaller banks to seek to get their money out as loans fall due, leaving major banks to handle the burden. We have the danger of a new kind of bank run—a run of smaller banks on their larger brethren. Large banks in the United States, Canada, Europe and Japan are on the back of a tiger from which it is proving somewhat difficult to dismount.

To the extent that attempts to dismount are made, it will tend to aggravate the difficulties of the deficit countries. The drift to shorter maturities is well-documented. This makes debt management problems doubly difficult and of course leads to increased front-end costs of borrowing. International lending, especially to developing countries, has slowed down. Private banks have a key role to play now and in the future. What must change, I believe, is the framework within which their commercial operations are conducted. Left to their own devices, the sum of their individual commercial decisions has created considerable problems for the private banks, their central banks and the governments involved. In a recent survey of this problem, Anthony Solomon, President of

the Federal Reserve Bank of New York concluded:

> "The starting point must be close collaboration among the governments and central banks of the major industrial countries. For debt burdened countries it means the willingness to work with the international institutions, especially the IMF. There also needs to be responsible interchange between private sector lenders and the authorities of borrowing countries."

I believe that there must be closer liaison between private sector banks and the Fund, with of course the approval of the borrower. Turning to official flows, or more particularly the rules and policies of the IMF, the first and obvious point to be made is the inadequacy of the resources available to the Fund in terms of the scale of the problem. Obviously, the news that the Group of 10 countries have agreed to support a proposal for a significant increase in quotas is welcome. I would expect that the Interim Committee will decide to increase quotas around 50 percent. Clearly this will help, as will the decision to extend the facilities of the General Arrangement to Borrow to countries other than the Group of 10. However, this is well short of the doubling of quotas many countries were calling for and which I believe was appropriate. Furthermore it will take some time even for this inadequate increase to be approved, country by country, and thus for it to operate. Another possible approach which will shock some purists is to segregate some current indebtedness of the chronically indebted countries and convert it into a special form of long term debt, guaranteed by the international community, bearing fixed interest payable regularly, denominated in marketable instruments. This would relieve those countries of the burden of refinancing short and medium term debt as well as the pressure of the risk of fluctuating interest rates. It would give the lenders a better security than they have at present, and help the private sector banking system to raise further funds for international lending with confidence. The second point to be made is that the Fund's approach to conditionality must be eased. These two observations are intimately related. Because of the revolving nature of the Fund, the conditions attached to its lending operations cannot be eased unless the Fund is given greater resources.

In advocating easier conditionality I am using one of those dangerous international codewords that invites misinterpretation. I am not urging international economic profligacy on a grand scale. Far from it. What I am suggesting is that the traditional pattern of Fund conditionality—that is, rapid adjustment to balance of payments health—is inconsistent with the nature of the structural balance of payments problems facing many countries. It is imperative that deficit countries be encouraged to develop longterm adjustment programmes designed to trade their way out of difficulties to the extent they can. They require that. The international economy requires that. The Fund's policies, conceived in the 1940s to deal with cyclical deficits, are not geared to do that.

Indeed after many years of attending Fund meetings, I have come to the conclusion that there is a profound lack of realism marking the debate over conditionality. Those who have argued for maintaining a tough conditionality have undoubtedly carried the day. What has been the result? Effective and tight discipline? Rapid adjustment and return to balance of payments equilibrium?

Quite the reverse. Countries do not turn to the Fund until it is almost too late. Instead they have turned to private sources of lending which have minimal standards of conditionality in the IMF sense.

I would argue, therefore, that the Fund's approach to conditionality has had the perverse effect of encouraging less adjustment overall than would have occurred had the Fund applied a more flexible and sympathetic approach to conditionality. I am interested in the effective results of policy stances—not the ideological rigour which accompanies them.

Ultimately there are grave political risks in all this. I had a letter recently from an old colleague of mine, a Prime Minister of a Commonwealth country, who said that if he had been silly enough to accept the short-term adjustment programme suggested to him by the IMF, he would have faced the prospect of riots in the streets and peasant farmers producing food only for their own use. If you object to anecdotal evidence of this nature, consider the case of Turkey. This was a country which adopted a stringent adjustment programme which led to the downfall of the government, followed later by the downfall of the new government followed by a takeover by the army. In another country army rule might not be so benign. I was astonished recently to see the Turkish experience held up to a U.S. Senate Committee as a success story. We have long recognised the linkage between economic liberalism and political liberalism. If we cannot devise a longer-term framework for adjustment that provides a credible policy response for democratic governments, we may well find that some countries will move inexorably away from democratic traditions. Severe austerity programmes and relatively open government are uneasy bedfellows.

It is a fallacy to suggest that for every country it is possible to make adjustments which would bring its external current account into balance and at the same time provide a standard of living which would be acceptable to people who are governed in a democratic tradition.

Another inadequacy I see on the institutional side is the absence of any effective provision for symmetrical surveillance. That is, countries in surplus must be encouraged to adjust in the same way that deficit countries are expected to adjust. There is implicit recognition in the Fund's articles of agreement on this but there is no mechanism in place to achieve the desired result. The concept itself is based on a fundamental accounting fact that for every dollar one country has in surplus another country has one dollar in deficit.

With sovereign governments, we are unlikely to ever agree on automatic balance of payment adjustment guidelines. I do see the need, however, for a body with much greater authority than currently exists to oversee this issue. It may be necessary, therefore, to consider setting up some sort of council, based in the Fund, with decision-making powers, as opposed to the Interim Committee which is an advisory body only. Such a council—which on occasions I have referred to as an economic equivalent of the United Nations Security Council—is in fact explicitly provided for in the 1976 second amendment of the Articles of Agreement of the International Monetary Fund. This provision has never been given the serious consideration it merits.

We must also find some means of introducing greater stability into the process whereby international liquidity is created. At various times during the past decade, the rapid and variable growth of international liquidity, principally in the form of externally held US dollars and other currencies, has given rise to proposals to operate a substitution account. This would provide a mechanism to enable countries to exchange their holdings of foreign exchange for SDRs. The objectives of this would be to moderate one major source of instability in the international financial markets and to make the international economy less sensitive to changes in the domestic economic policies of the major countries.

I am not suggesting there are not difficulties in this proposal—just as there are with achieving an effective system of symmetrical surveillance. However, they are typical of the key issues that sooner or later we must examine in the context of the international trade and payments system as a whole.

Turning finally to aid flows, one can say simply that the volume of development assistance has remained stable at about $25 billion in nominal terms for several years, implying a substantial real decline. It is easy to label aid flows as wasteful or unproductive. Properly managed, they can contribute to the development process. New Zealand's own aid programme which is so very small in absolute terms, but which is most effective in the context of the tiny island states in the South Pacific, is one reason why I cannot accept the prevailing modern view on aid.

Looking at the position of the very poorest countries which will be quite unable to maintain absolute minimum standards without increased aid flows is another reason. We have to accept that democratic parliaments in present circumstances are not going to vote substantially increased amounts for either bilateral aid or multilateral aid. Given this disenchantment with aid, we are going to have to look at global mechanisms, such as the proposal to link Special Drawing Rights to international aid. We are going to have to look at measures which in effect tax the world community. One result will be an easing of the political tension in respect of aid proposals in the donor countries. If we are going to increase international liquidity by issuing SDRs, why not issue them as aid, rather than giving the wealthy countries that do not need them the lion's share. This then is how I read the present position relating to the payments side of the trade and payments equation as it has developed since the collapse of key elements of the Bretton Woods system. What about the trade side?

I do not wish to spend a lot of time discussing the evils of protectionism. At meetings such as this, protectionism represents a soft target. We can all deplore it because we all know that protectionism is something done by others, not ourselves.

What I would like to do is to analyse the *linkage* between protectionism and the critical financial issues I have just described, because it has a direct bearing on my central conclusion: namely that we need a second Bretton Woods type conference to examine the international trade-payments system as a whole.

To set the scene, let me quote the concluding comments of the annual GATT Study of International Trade published late last year:

> "The gradual but continuing accumulation of restrictions on international trade of course poses a threat to the multilateral trading system . . . . but the more immediate danger may be that it will trigger a severe disturbance in the already troubled international financial system. This danger was demonstrated in the decade of the Great Depression."

Financial dislocation and protectionism feed on each other. Take, for example, the impact of erratic changes in exchange rates on trade policy. I read recently the comments of the respected liberal international economist who observed that if Adam Smith were alive today and observed the recent exchange rate fluctuations he would have been a protectionist. The fact is that wild fluctuations in exchange rates bring about unpredictable and sometimes temporary shifts in comparative advantage. They make a nonsense of any residual protection system that relies upon tariff protection at the frontier. The magnitude of the swings quite outweighs the economic significance of the generally low tariff rates now prevailing as a result of the successes of the Kennedy and Dillon negotiating rounds in the GATT. I believe that this is part of the reason for the growing propensity of countries to resort to non-tariff barriers.

There are now over 600 different types of non-tariff barriers ranging from the so-called 'voluntary' restraint agreements through to local content requirements, variable import levies and so forth. The fact is that international trade is becoming less and less governed by the principles and rules formulated by the original negotiations of the GATT. One estimate I have seen is that by 1980 almost 50 percent of trade by all market economies was 'managed' trade—that is, trade which is not, for a variety of reasons, governed by the conventional forces of the arms-length free market.

The linkage between protectionism and financial dislocation goes deeper than this however. Ultimately, loans have to be serviced from export earnings. If trading opportunities are cut back, financing becomes a riskier business. As is suggested by the increasing talk of devices such as selective safeguards, protectionism is a particularly acute problem for those countries which have shown a marked competitive edge in certain sectors. When protectionism cramps the opportunities for investment in competitive export-oriented projects, it undermines the stability of the investment itself.

All the orthodox advice each country receives from its own advisers, from practical men of business and international experts, is that it must export more and, import less to deal with its financial difficulties. Simple arithmetic, however, shows the short-sightedness of this. The result of each individual country following this article of faith is a reduction in world trade and growth. That is exactly what is happening today. We may, however, be seeing the early signs of a shift in the international community's thinking on this. The OECD consensus for example is now clearly that the risks of inducing a further retrenchment of the world economy exceed the risks of a renewal of inflation. As was apparent from the Group of 10 meeting in Paris, the major countries are now more and more emphasising the need for co-ordinated expansionary policies. In my view, these need not reverse the gains made in reducing inflation.

It remains to be seen whether this will lead to a rethinking of the role of developing countries. In 1980, nearly one quarter of the exports of the industrial countries went to developing countries in terms of manufactured exports the proportion is about one third. The economic welfare of industrial countries thus depends increasingly on the developing countries being given the opportunity to trade their way out of difficulty.

If the developing countries have to tighten their belts, not only do their standards of living fall, but the exports, and thus the production, and thus the standards of living of the wealthier countries also fall. Additionally, those of their citizens who have invested in external loans may lose their money.

We have just concluded the GATT Ministerial meeting—the first for many years. Each country has walked away from that meeting applying a different set of adjectives to the same outcome. These descriptions range from 'realistic', 'preserving the basis for future discussions', to 'a failure'. I am awarding no prizes for attempts to match countries to these descriptions. It is all too familiar, I am afraid.

Call it what you will, it is manifestly clear that the post-war political mandate of the GATT is all but exhausted. That mandate was, primarily, to reduce tariffs on industrial goods. It has accomplished that with great success. In respect of agricultural products it has been a monumental failure. But the GATT is stymied by the fact that the key contracting parties are not prepared to use the framework of the General Agreement to deal with the trade problems of the eighties and nineties, let alone to explore the relationship between payments and trade. As with the International Monetary Fund, the GATT is operating with the remnants of a constitution designed for the problems of the 1940s. Both institutions need constitutions geared to the problems of the 1980s and beyond.

This brings me to the conclusion which I set out for your consideration at the start of my address. I believe that we need a broad-based reappraisal of the trade and payments system to establish a dynamic and liberal framework for international

economic relations for the remaining decade and a half of this century. This will be a formidable task, but the first requirement is political recognition of the need for such an appraisal.

The current international forums seem to me unlikely to produce the broad-based appraisal required. The North-South dialogue is not framed for an effective consideration. The problems of slow growth, protectionism, financial dislocation and debt are so closely connected that no institution can of itself forge the consensus necessary. The summit meetings of the wealthy countries may agree on an analysis, but agreement on action trips over the fact that one or more of them are always facing an election in the immediate future.

There are no easy answers and hard adjustments to economic reality will be required. My contention is that it is likely to prove easier for governments to face these adjustments if they can say to their peoples that other countries are moving in concert—that the decision has been agreed by the world community. This is an extension of a simple enough proposition in the trade field: namely, that multilateral trade liberalisation is politically feasible where unilateral trade liberalisation is generally not. Individual reforms are more manageable, more readily accepted as logical and necessary if they seem as part of a new strategy, covering the broad spectrum of trade and payments issues. The operations of the post-war institutions have tended to unravel the tight connections between trade and payments. The theme of my arguments is that the purpose of the next international review must be to put them together again.

The significance of Bretton Woods is that, because we were sufficiently scared, it created opportunities to break the political logjam on the policies that had caused so much harm to international co-operation in the 1930s. Some four decades later, I believe we are facing a comparable political logjam on the trade and payments front. After Bretton Woods each country had to ask itself: this is what the world community had decided. Now are we in or are we out? At the end of the day, the vast majority of mixed economies decided there was only one answer to that question. Unless we begin the first political steps towards a comprehensive examination of the present world trade and payments system, we shall simply have to accept whatever the existing framwork for international economic relations deals out to each of us. In that event, I must be totally pessimistic about the future of international economic co-operation and, indeed, the future of the world economy itself.

What I suggest is a conference, not of a day or two, but for as long as it takes to reach a consensus, many weeks perhaps. There will be many more sovereign states than at Bretton Woods, but no consensus will be reached unless the powerful countries concur.

All this will take time. The amount of time that today's band aid solutions can buy us is limited. The basic illness remains and will continue to worsen.

P. D. HASSELBERG, GOVERNMENT PRINTER, WELLINGTON, NEW ZEALAND—1983

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