NORTH-HOLLAND

North American Journal of
Economics and Finance 11 (2000) 77–104

THE NORTH AMERICAN
JOURNAL OF
ECONOMICS
AND FINANCE

Dismantling the cross of gold: economic crises and U.S. monetary policy

Daniel J.B. Mitchell*

UCLA, Anderson Graduate School of Management and School of Public Policy and Social Research, Los Angeles, CA 900095-1481, USA

Received 21 November 1999; received in revised form 4 March 2000; accepted 4 March 2000

How can a U.S. Gold Commission attempt to determine the role of gold in domestic and international systems without there being any foreign participation? . . . Audience question at the World Conference on Gold, Rome, Italy, February 1982 (Jastram, 1983)

Abstract

The advent of the Euro has put the spotlight on international monetary policy. Could a new world currency be created? Could there be a return to international fixed exchange rates? The history of the American response to the gold standard in its various forms suggests one theme. At key moments during the 20th century, the U.S. chose domestic monetary sovereignty over international obligations. This address traces the history of American attitudes toward gold from the 1890s to the present. That history suggests that creation of any currency system requiring loss of U.S. national monetary sovereignty is most unlikely. © 2000 Elsevier Science Inc. All rights reserved.

JEL classification: F33; N11; N12

Keywords: Gold; International monetary arrangements

* Tel.: +1-310-825-1504; fax: +1-310-829-1042.
E-mail address: daniel.j.b.mitchell@anderson.ucla.edu (D.J.B. Mitchell).

PII: S1062-9408(00)00028-0

1. Introduction

With the creation of the euro on January 1, 1999, much of the European Union's economy was united under a single monetary system with a common central bank. Existing currencies of the member states—such as the French franc, the Italian lire, and the German mark—became mere fractional representations of the euro on that date and will eventually disappear. European monetary unification eliminated the risk of exchange rate fluctuation from cross-border trade and investment flows within the euro zone. The development of the euro in the EU raises the question of whether similar currency unification could someday occur within other currency blocs such as NAFTA (or an expanded version of NAFTA if other Latin American countries become part of the agreement).

Indeed, the euro's creation raises an even larger question. Could the European experiment lead to creation of a world currency some time in the 21st century? Given the experience with flexible exchange rates during the 1980s and 1990s, this question is surely worth considering. The U.S. dollar appreciated dramatically for the first half of the 1980s in what seems in retrospect to have been a speculative bubble. At the dollar's peak, the U.S. ran a massive trade deficit and a variety of domestic trade-sensitive industries suffered injuries due to the artificial boost in their cost structure relative to world competition. During the second half of the 1980s, the process unwound as the dollar fell in value. Still more dramatic were the Mexican peso crisis of 1994 and the Asian financial crisis that began in 1997. Both of these crises featured substantial depreciation of the affected countries' currencies and severe macroeconomic effects within those nations. These episodes raised questions about the impact of global financial markets and especially about the policies and authority of the International Monetary Fund (IMF).

Since the early 1970s, the world has not really had a monetary "system." Rather, countries have followed their own approaches to managing their currencies. Some have allowed a relatively free float with little official intervention. Others have tied themselves to the dollar or some other currency or to a basket of currencies. The rigidity of these linkages has varied. Some countries have used currency boards and abandoned independent monetary policy entirely whereas others have followed an active intervention approach. Crawling pegs and varying degrees of managed floating have also been part of the currency mix. The IMF's role in this currency smorgasbord is ambiguous. That institution was created in 1944 to oversee the workings of the Bretton Woods system of fixed exchange rates, arrangements that ended abruptly in 1971. Could the IMF—now an institution without its original mission—become a world central bank in some new international currency system? Or will it remain a relatively weak institution, constrained by limited resources, complex and arcane procedures, and cumbersome decision making?

The theme of this paper is that to the extent that U.S. assent is needed, major steps toward a world currency or even a fundamental shift towards greater IMF supervisory authority is unlikely. Even a formal NAFTA currency zone is improbable unless the partner countries agree to American-made and American-based monetary policy. American history is at the root of this opinion. IMF weakness—for example—is a product of U.S. history, a history that goes back to the 19th century. Put more directly, the specter of William Jennings Bryan—the unsuccessful Democratic candidate for president in 1896—still haunts the international