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Balancing act: Negotiating global needs and national sovereignty under the Bretton Woods regime

Similar to the manner in which domestic law must balance individual liberties with collective interests, any international policy framework must balance the sovereignty of individual nation-state actors against certain global priorities of the so-called international community. Recent world history has been a constant back and forth shifting of this balance as nation-states choose whether to accept or reject the prevailing global order and as new methods of incentivizing or coercing participation evolve. Studying the ways in which differing arrangements of this balance have led to varying degrees of democratic participation within states, varying degrees and distributions of economic prosperity, and varying types of international conflict is thus an important academic task. What exactly is the role of the nation-state in relation to the larger international policy framework, and how have policies been crafted which successfully manage this balance?

One of the more successful eras in the history of coordinating national and international interests was the postwar period now known as the Golden Age of Capitalism which emerged from the framework of the first Bretton Woods system. Though the world was left in shambles after the worst war in history and political tensions were high, the period following the war and up until the early 1970s was one of fairly generous economic growth and stability. Rates of growth averaged between four and five percent through the 1950s and 1960s while closer to only three and two percent in the 1970s and 1980s respectively (Marglin & Schor, 1991). Furthermore, the rise in each quintile of family income levels in the U.S. was between 99% and 116% from 1947 to 1979 indicating widespread new prosperity. By comparison, from 1979 to

2000 the lowest quintile of family income increased by only 3% and the upper quintile by 53%.

An essential feature of the Bretton Woods regime which gave rise to this growth was the way in which it managed the divide between national sovereignty and global priorities. Bretton Woods contributed to increased international integration by creating a large fund known as the IMF which member countries could draw on to correct short-term balance of payment disequilibria. This facilitated stable exchange rates and trade at the international level without the need for immediate and drastic domestic measures such as depression. Bretton Woods also instituted a par-value system of fixed exchange rates and capital controls which helped shelter countries from speculation and allowed for pursuit of domestic economic priorities. All of these mechanisms were so instituted as to impose some discipline on member countries, but not in such an absolute manner as to completely reduce national sovereignty. The success of this balance was profound. Through creation of a flexible international policy space which managed the tension between the sovereignty of nation-states and the need for some global order, the Bretton Woods system created an environment for increased global economic integration without wholesale erosion of the ability of a people to govern themselves at the national level.

The Importance of National Sovereignty

For the past few centuries, sovereign-nation states have formed the cornerstone of the majority of political organization. Karl Deutsch (as cited in Horsman and Marshall, 1994) explains that “the nation-state offers most of its members a stronger sense of security, belonging, or affiliation, and even personal identity, than does any alternative large group” (p. ix). This sense of national belonging has both positive and negative outcomes. The experience of the world wars of the Twentieth Century revealed an ugly, competitive side of belonging to a nation-state. Nation-states became tools for promoting ideologies which oppressed minority constituents and othered those who belonged to different countries. The nation-state was a blade for dividing. On the other hand, the nation-state can also be a positive force, providing people with a purely political point for democratic organization, decision-making, and unity in common interest. John Ralston Saul (2005) writes that "the positive form of nationalism is tied to self-confidence and openness and to a concept of the public good" (p. 245). Both the positive and negative aspects of national-sovereignty were vividly present in the minds of those crafting the postwar economic recovery plans which emerged as the Bretton Woods system.

On the one hand, it was broadly accepted that the economic turmoil of the interwar period contributed greatly to the political turmoil which launched the Second World War. Therefore Keynes, White, and the other architects of the postwar economic regime felt that ensuring a substantial degree of international economic stability would be paramount to ensuring political stability and vice-versa. The result was a strong imperative to make a robust, coherent global system which could mute the negative aspects of nationalism. The Bretton Woods framework was thus designed to prevent national sovereignty from inspiring excessive trade protectionism or competitive devaluation.

On the other hand, they also recognized that postwar reconstruction would require a tremendous level of internal autonomy in rebuilding domestic economies. Keynes was also a strong believer in the notion that economies should be so structured as to allow nations to undertake their own economic development initiatives. As he famously wrote,

> We all need to be as free as possible of interference from economic changes elsewhere, in order to make our own favourite experiments toward the ideal social republic of the future; and… a deliberate movement towards national self-sufficiency and economic isolation will make our task easier, in so far as it can be

> accomplished without excessive economic cost. (as cited in Best, 2005, p. 41)

There was a further concern that if nations were too tied in with an international economic policy regime and if it went too strongly against their perception of their own national interest, then these nations might be inclined to withdraw and bring the whole international order crashing down once again. Therefore it was of paramount importance that the positive sides of nationalism and the organizing potential of the nation-state be preserved to some extent.

Balancing the National and International Under Bretton Woods

With such thoughts about the sovereignty of the nation-state in mind, the visionaries of Bretton Woods set about crafting an international policy framework which could successfully manage the duality of nation-state and international community. It was no easy task. As Jacqueline Best (2005) writes,

> It would be a liberal, multilateral system, in order to avoid the painful tariff wars and competitive devaluations of the interwar years, and it was to be a full-employment system in order to avoid the costs and dangers of domestic economic and political instability. This was an ambitious undertaking, because the world had never before managed to combine both goals in a single international economic regime. (p. 33)

This did not deter Keynes in Britain and White in the United States who, before the Second World War even ended, had already envisaged and furiously debated plans for a new international economic policy framework. The resulting scheme balanced sovereignty of the nation-state with global priorities in four main ways.

The first was through establishment of fixed but adjustable exchange rates in the par value system. The International Monetary Fund, "in consultation with" the member countries, would establish fixed exchange rates which the countries were obligated to maintain within plus or minus one percent of parity. Adjustments could be made to the exchange rate only in order to correct a "fundamental disequilibrium," however this was to be done cooperatively with the IMF, providing for a certain degree of international authority. National sovereignty was given some supremacy though, for small changes to the par value of less than ten percent could be made unilaterally and the IMF would be powerless to dissent (Best, 2005, p. 53). It would also be unable to dissent on the basis of "domestic social or political policies of the member proposing the change," providing yet another measure of national autonomy within the system (Gardner, 1980, p. 115). To balance this, the international community represented in the IMF could, by two-thirds vote, engage in open criticism of a member nation's actions by issuing a report at any time "regarding its monetary or economic conditions and developments which directly tend to produce a serious disequilibrium in the international balance of payments" (Gardner, 1980, p. 115).

The second major feature in the Bretton Woods system was provision of balance-of-payments loans and liquidity through the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development (IBRD). The IBRD was created to meet long-term credit needs during reconstruction. The IMF was established to finance short-term balance of payments deficits. Quotas were established for each member country reflecting their economic size, and members were allowed to draw on the fund in an amount commensurate with their quota. Providing this short-term credit allowed for increased national and international stability both, because fixed par values could be maintained and countries would not have to induce depression to maintain the current account balance.

With relation to these two funds, the major issue impacting the balance between sovereignty of the nation-state and global priorities was the debate between conditionality and automaticity. Automaticity meant that a country's right to draw on their quota would be mostly automatic, whereas conditionality implied it would be subject to the discretion of those managing the fund. In this debate, Keynes argued fiercely for automaticity whereas White was concerned about how the largely American-funded resources would be used. In the end there were again aspects which supported international authority and others which gave sovereignty to the nation-state members. There was an underlying notion of automaticity in that the framework said countries "shall be entitled" to buy currency (Gardner, 1980, p. 113). This was tempered, nonetheless, by a provision for the larger international community, declaring that "the IMF retained the right to declare a state ineligible to use its resources if it determined that the member was using those resources 'in a matter contrary to the purposes of the Fund'" (Best, 2005, p. 52). Furthermore, members with outstanding balances exceeding their quota or members who were persistent creditors both faced charges and constraints, providing another check on runaway national autonomy. Therefore the second major feature of Bretton Woods—the creation of IMF and IBRD funds—also incorporated and delicate balance between granting nation-states sovereignty and imposing international rule.

The third manner in which Bretton Woods was able to manage the tension between national and international interests was through management of convertibility and capital flows. While convertibility of current account transactions was an important goal of the system to help facilitate free trading, "the IMF statutes granted each member country the right to control capital movements as it saw fit" (Voth, 2003, p. 257). Capital flows were greatly feared after the interwar period for their destabilizing effects on domestic economies. This provision was as clear an example as any that Bretton Woods was carefully tailored to balance both the internal and external constraints on national economies, for as Krugman (2004) explains, "By insisting on convertibility for current account transactions only, the designers of the Bretton Woods system hoped to facilitate free trade while avoiding the possibility that private capital flows might tighten the external constraints faced by policymakers" (p. 549).

The final major tool of the Bretton Woods regime for balancing national and international demands was an advisory role of the IMF in domestic policies. As mentioned earlier, following a two-thirds majority vote, the IMF members could issue a report to a country regarding management of its economic positions. In addition to this power, Article XIII allowed the IMF to "require members to furnish it with such information as it deems necessary for its operations" (Best, 2005, p. 53). These two key measures coupled with the limited amount of control over fund use and revaluation wove an element of supranationalism into the Bretton Woods regime without thoroughly undermining autonomy of the member nation-states.

Putting Bretton Woods Policies into Practice

Within this framework of checked national and global interests, the world saw nearly a quarter century of widely distributed growth as well as reasonable political stability in the West. While it is clear that the institutions which Bretton Woods founded had various provisions meant to strike a balance between the nation-state and international community, it is important to examine how things *actually* functioned over those two and a half decades of success. What kinds of dynamics developed in the actual implementation of Bretton Woods and to what degree were they responsible for its success? There are two main interpretations.

First, in *The Limits of Transparency* Jacqueline Best advances an argument that the fundamental ambiguities of the Bretton Woods system between the poles of supranationalism and nation-state sovereignty played a constructive role because they created a policy space which was flexible and often ad-hoc. The result was “an ongoing process of interpretation and negotiation” (p. 58) which made the system adaptable enough to endure for many years.

Best supports her argument by highlighting the numerous vague, ambiguous, and indeterminate aspects of the plan which emerged from Bretton Woods. “Although many thousands of words were written in forging this agreement,” she writes, “the final document left much unstated, and thus open to interpretation” (p. 56). One such area was in determining whether debtors or creditors would bear the responsibilities of adjustment. While clearly spelled out in the Keynes and White plans, the final agreement did little to cover the issue (p. 56). Other gray areas included the use of capital controls and the scope of the IMF’s discretionary powers. The ambiguity is further evident in the extraordinarily vague wording used in the agreement, such as “fundamental disequilibrium” and “in a matter contrary to the purposes of the Fund.” Best concludes that these measures meant that “the tension between particularist and internationalist tendencies within Keynesian theory were translated into the final document” (p. 56).

The result of a somewhat ambiguous policy framework was, in Best’s view, a system which often functioned from case to case and adapted as needed, all the while operating within some more rigid guidelines. In this manner, it successfully reconciled a fundamental danger of any international institution: an unyieldingly strict system could be so unforgiving as to be abandoned by its nation-state constituents, and an overly loose system would fail at accomplishing its policy objectives. As articulated by Best (2005), “The Bretton Woods regime began its life as an open and negotiable set of policies and institutions and continued in that spirit for quite some time, seeking to reconcile its overarching principles with the particular and changing needs of its individual members” (p. 59-60). In this way nation-states could remain cooperatively committed to the international system while also looking after their own interests at certain times.

A competing argument suggests that Bretton Woods was successful not so much from the balancing of various interests but rather from the hegemonic influence of the U.S. in imposing and maintaining the system. Best (2005) calls this interpretation of the Bretton Woods regime a power-based analysis and explains that supporters of this position "have emphasized the key role played by U.S. hegemony in forging, sustaining, and finally eroding the stability of the Bretton Woods regime" (p. 18).

Supporters of this position are especially inclined to point toward the significant role the U.S. had in shaping the framework of Bretton Woods and also in precipitating its collapse. Harold James' account of the postwar economy states rather bluntly that "the initiative for the opening of the world economy after 1945 came largely from one country, the United States" (James, 1996, p. 606). Indeed, many decisions made during the negotiations over Bretton Woods do come about somewhat unilaterally from the United States. One obvious instance was in the setting of the overall size of the Fund; the original Keynes proposal was for resources of at least $26 billion while the final agreement was only $8.8 billion upon U.S. insistence (Gardner, 1980, p. 112-113). Another example was the eventual decision to hold the U.S. dollar as the reserve currency, which happened "by an apparent sleight of hand" (James, 1996, p. 50). Harold James also argues that U.S. support of Bretton Woods was so paramount that "when at the end of the 1960s the United States began to view the dollar… as a national resource to be manipulated for the sake of national advantage, the system soon collapsed" (p. 591). All these arguments emphasize the hegemonic role of the United States as the dominant force functioning in the Bretton Woods system.

As with so many things, reality probably lies somewhere in between the ambiguity theory and the theory of a dominant U.S. influence. It's hardly defensible to say that ambiguous guidelines played no role in the operation of the Bretton Woods system, for there are many examples such as the Dollar Gap and the process of returning to convertibility which involved case-by-case negotiations and a great degree of flexibility. On the other hand, the influence of U.S. hegemony is also undeniable every step of the way.

A better understanding might be a more holistic view that all members of the Bretton Woods negotiations including but not limited to the United States were committed to a somewhat ambiguous policy framework. In this sense, buy-in to the system by the U.S. was a necessary but not sufficient condition for the system to produce such successful results. Yes, the regime relied heavily upon support from the U.S. to function (the U.S. has always had by far the largest quota and been undeniably influential in governing the institution), but the U.S. did not use its influence to constantly impose its will upon other countries. Rather, the U.S. frequently played a leading role in creating the flexible, sometimes ambiguous policy space which characterized Bretton Woods and allowed for the balance between national sovereignty and international rule. The conviction among U.S. leaders at the time seemed to be that postwar stability worldwide, especially in light of the Cold War, was a key national security interest of the United States (evidenced especially by the Marshall Plan). Harold James (1996) alleges that it was in part thanks to the work of U.S. lawyers at the Bretton Woods conference that some of the agreement became intentionally ambiguous. He notes that the U.S. National Advisory Council on International Monetary and Financial Problems (NAC) later openly recognized that "the obscurity of the language is deliberate" (James, 1996, p. 55). It was thanks to such ambiguity and benevolent U.S. support that the Bretton Woods framework was able to negotiate the national-supranational sovereignty divide so well, both imposing some degree of international order and allowing for nation-states to self-govern.

Rise of the Neoliberal World and Erosion of the Nation-State

The Bretton Woods system which ushered in such an extended period of widespread growth and stability began to collapse by the late 1960s and especially into the 1970s. Sometimes it happened gradually, while at other times dramatically such as the 1971 decision to let the U.S. Dollar float. If it was a successful balance between national and international interests created through an ambiguous policy framework which characterized the Bretton Woods era, it was a decided tip away from national economic policy autonomy for much of the world and a brash assertion of U.S.-dominated interests which marked its demise.

All sorts of observations have been made pointing out factors which contributed to the decline of the system formulated at Bretton Woods. The famous Triffin Dilemma argued that with the U.S. dollar as a key currency, either there would be a liquidity shortage or the U.S. would have to run large deficits to provide ample dollar reserves. Triffin predicted crisis at such time as it becomes evident that dollar reserves exceed U.S. holding of assets. Others factors blamed for the decay of the system include refusal to devalue the U.S. dollar and a decline in U.S. political interest in supporting the system (James, 1996, p. 591). Rapidly increasing flows of international capital are also perhaps the most widely cited factor. Sometimes these changes came about by a deliberate skirting of domestic policy autonomy while other times they happened when states willingly relinquished power to market forces and international authorities.

In one key example, the late 1950s saw the emergence of the Euromarkets in which U.S. dollar denominated securities were traded in European markets offshore from U.S. regulation. Best (2005) notes that, “they were not so much created as stumbled upon, as bankers first discovered and then exploited a series of loopholes in the complex web of postwar financial regulations" (p. 105). The Euromarkets became ideal grounds for transferring enormous amounts of speculative international capital which threatened to disrupt domestic economic policy efforts. While these markets clearly weren't a part of the original Bretton Woods framework, some authors such as Eric Helleiner (1994) have argued that they "could not have survived without the backing of Britain and the United States" (p. 8). In other cases a *deliberate* embrace of liberalized finance by states was clear.

On numerous occasions between the late 1960s and early 1980s policymakers rejected talk of imposing capital controls. Helleiner identifies several such cases. The first was when speculative flows so severely threatened the fixed exchange rate system that Western Europe and Japan proposed capital controls between the "throughflow" countries of the Euromarket system but U.S. opposition doomed the plan (p. 10). Subsequent cases in Britain and France of proposed capital controls were rejected domestically "after extremely divisive internal debate" (p. 10). Japan, Switzerland, and many others also later followed suit. Helleiner offers several hypotheses to explain why states began to buy in to liberalized financial regimes. He highlights neoliberal arguments that liberalization promotes freedom and efficiency, eroding support for current paradigms in the face of economic slowdown, and fear of being left behind in a new global economic order (p. 12-17). In *The Collapse of Globalism*, John Ralston Saul echoes Helleiner's final point with an interesting argument that advocates of neoliberal economics reasoned with "the force of declared inevitability" (p. 3) and uses the phrase "economic determinism" (p. 28) to describe the force driving states to relinquish power to the markets.

The rejection of capital controls and embrace of neoliberalism led to an erosion of national autonomy in favor of international finance. Freely moving flows of speculative capital could undermine a country's balance of payments deficit or balloon a surplus and overwhelm the ability of central banks to conduct domestic monetary policy. Horsman and Marshall (1994) declare bluntly that "the expansion of the international marketplace has made the pursuit of national economic goals impractical" (p. xx). The United Nations Conference on Trade and Development (UNCTAD) echoed this in a recent presentation which stated that "the tension between international commitments and national policy flexibilities has intensified. Progressive liberalization of capital, financial and trade flows and increasing role of transnational firms have weakened impact of national policies." The weakening of the nation-state's autonomy paved the way for the era of globalization in which large international policy bodies and transnational corporations became increasingly dominant.

Conclusions: In Absence of Strong Nation-States

The Bretton Woods system was designed as a flexible policy space to balance national and international interests in the postwar world. Its architects were well aware that economic and political stability are linked. Allowing nation-states some autonomy in managing their domestic economies would promote political stability within nations, and imposing some degree of international economic order and rule would foster trade and international cooperation. The globalized world order which followed Bretton Woods has overlooked the importance of the economic-political link at great expense. The territorial nation-state provided the world with somewhat arbitrary, primarily political points for organization, and the subsequent decline of the nation-state in the face of globalization has created a vacuum for this type of domestic mobilization. In its absence, several possible alternatives have emerged, but none very successfully.

Some political theorists such as David Held argue that "democracy has to be a transnational affair" (as cited in Panitch, 2004, p. 11). The idea is that if the policy setting and decision making that impacts citizens is now being done at a global level, then democratic participation and civil society should scale up to that level too. Unfortunately getting the people of the world to buy in to large global bodies often proves difficult. As Horsman and Marshall (1994) put it,

> Despite the advent of the 'global village', individuals so far feel little more than token allegiance to emerging supranational bodies such as the European Union. There is as yet no sense of 'belonging' to an efficient superstate. Where is the reflection of self, of the group, of the nation? (p. xiv)

Movements such as the 1999 WTO protests in Seattle and the 2009 efforts in Copenhagen have shown that democratic mobilization at a global level has so far been only minimally effective and usually dwarfed by the much more massive resources of global political institutions and transnational corporations.

If transnational democracy proves ineffective as a means of political organization in a globalized world, some fear that cultural, religious, and ethnic identity may fulfill the role. Horsman and Marshall (1994) point to the former Yugoslav state for an example of the hazards this creates:

> In Sarajevo, the capital of Bosnia, Muslims, Croats and Serbs lived together, often side by side in the same apartment block. The dissolution of the Yugoslav state created a vacuum filled quickly by tribalism, and a battle waged among imagined communities with all the fury that references to common culture and history can inspire (p. 187)

Ethnic and other forms of splintering have historically been all too common a response to weakening nation-states.

Finally, an alternative response could be an aggressive reassertion of nationalism and backlash against globalism. This is precisely the type of situation that Keynes, White, and the other creators of the Bretton Woods system wished to avoid in creating an international policy framework which allowed for a healthy balance of power with sovereign nation-states. John Ralston Saul (2005) points to China, Brazil, and India as examples of nations aggressively re-asserting themselves, developing economic capacity, and often doing so in the face of traditional Western powers (p. 232-233). This fear of rising nationalism of the aggressive sort is furthered by the response of the United States, Britain, and other large nations who frequently seem to berate China and growing nation-states for failing to play by their rules.

Clearly a workable alternative is needed to prevent the world from going back down the path of political and economic fragmentation which led to the first two world wars. In searching for such a solution, it is paramount to remember the complicated relationship between politics, economics, national sovereignty, and international rule which characterize our interconnected world system. Exactly how the world can create a new regime to manage these dynamics in the face of present-day globalization is something policymakers, academics, and citizens will have to study intensely, but they should not forget the successful aspects of the Bretton Woods system in ensuring a period of relatively broad prosperity and stability throughout much of the globe. The world emerging from World War II had endured atrocities seemingly unthinkable even today, and was in many ways far more fractured than the present global community. Although it will be a challenge, there’s hope that through increased democratic participation in global policy institutions, superior balancing of national priorities with international interests, and perhaps through innovative new policy frameworks we might realize a world which builds and improves upon the successes seen during the Bretton Woods era in the decades following the world wars.

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