
Fred Bergsten and the Institute's Work on Exchange Rate Regimes

JOHN WILLIAMSON

When the Institute for International Economics started functioning in the second half of 1981, I recall being surprised at hearing Fred Bergsten predict that the dollar would continue appreciating and the United States would go into a big current account deficit. Personally, I don't believe in forecasting exchange rates, but I have to say that he was right on both counts. Those deficits have cumulated into a large net debtor position for the United States. Despite his love for the dramatic, Fred has never tried to imagine these debts away by postulating the existence of dark matter. Instead, he argued that deficits and debts posed a policy problem, to which we at the Institute sought a solution. A part of that solution (an important part, but he has always been clear that it is only a part) involved the exchange rate.

In this paper I trace the development of thought at the Institute on the exchange rate regime and the other arrangements that should complement it. I explain the intellectual background to these proposals and how they were related to other major intellectual developments of the period.

Perhaps I should say a word in this introductory section about the role of particular individuals and whether there is such a thing as an "Institute position" on such questions as the exchange rate regime. It is quite clear

John Williamson, a senior fellow at the Institute, has been associated with the Institute since 1981.

that there are no formal Institute positions; we have (mercifully) no vision statement to which new (or old) employees are required to subscribe. At the same time, it is difficult to imagine that a rabid protectionist, or someone who regarded the international financial institutions as either agents of imperialism or threats to the future of the United States, would feel comfortable applying for a job here, or would be likely to be appointed if he did. Within the ambit of a broad internationalist perspective, Fred has made a conscious effort to preserve a nonpartisan and eclectic reputation for the Institute. Not all of my colleagues subscribe to the views on exchange rate management that Fred or I (as the principal writers on this subject) have advanced: Indeed, Fred has not always endorsed my positions on these issues, as I will elaborate below. If Fred or I made more noise than anyone else about target zones, then it's possible the world identified the Institute with the target zone proposal. That is life, but it was not policy.

History

Fred Bergsten had been one of the leading advocates of moving to limited flexibility of exchange rates in the period prior to the breakdown of the Bretton Woods system (see Bergsten in Halm 1970). My own advocacy in that period had been focused exclusively on the crawling peg, rather than also embracing the wide band proposal. As it turned out, however, the world moved to floating rates rather than any form of limited flexibility. At the time, Fred and I both felt that the change to floating rates went too far and that the world would have been better off with an intermediate regime. The design of such a regime has been one of our continuing pre-occupations since then.

The first venture of the Institute into the exchange rate issue was a joint paper that Fred and I wrote for the Institute's second conference, held in 1982, on Trade Policy in the 1980s (Bergsten and Williamson 1983). We argued that it was a mistake to analyze trade policy in isolation from the exchange rate issue: This mistake rested on an implicit but incorrect assumption that prolonged misalignments of exchange rates would not occur. In addition to their direct and obvious effect of fomenting trade imbalances, misalignments would widen the coalitions damaged by liberal trade and lend them some legitimacy and thus foster protectionist sentiment.

We distinguished three concepts of the equilibrium exchange rate: fundamental equilibrium (defined, with a glance over our shoulder at Bretton Woods, as the average rate over the cycle that would reconcile internal and external balance), current equilibrium (the fundamental rate modified to reflect cyclical forces), and market equilibrium (no intervention). Misalignments were defined as major and prolonged departures of the exchange rate from its fundamental equilibrium value. We discussed the role of the

periodic yen/dollar misalignments in generating economic tensions between the United States and Japan. The climax of the paper was the enumeration of three strategies for exchange rate management intended to avoid misalignments: pegging with monetary policy subordinated to maintaining the peg, floating “with target zones or reference rates,” and employing capital controls. In the first two cases it was envisaged that the nominal rate would crawl so as to maintain the real target constant. These strategies were not examined in detail, but one important additional point was made. It was acknowledged that an attempt to pursue a real exchange rate target could be destabilizing, in the same way that pursuit of a target for the real interest rate or unemployment could destabilize the economy. The key to avoiding such instability is to set a target consistent with stability and to adjust it promptly if evidence suggests it has been set wrongly.

Target Zones

As just noted, the pioneering paper by Fred and me did not focus on how a target zone system (or one based on reference rates) might function. But Fred recognized the importance of the issue and set me to work on it immediately. My first thoughts were published in September 1983, in one of the Institute’s early Policy Analyses, or PAs (Williamson 1983, revised in 1985). I again drew the distinction between market, current, and fundamental equilibrium and defined misalignment (now sharply distinguished from volatility¹) as prolonged departure of the exchange rate from its fundamental equilibrium. I attempted to measure the fundamental equilibrium exchange rates (FEERs) of the five major currencies of the day (US dollar, deutsche mark, yen, pound sterling, and French franc) and thereby to quantify misalignments. I diagnosed the costs of misalignments so as to build a case for managed exchange rates. But the heart of the paper was the first blueprint for a target zone system, which was laid out in a section called “Techniques of Exchange Rate Management.” I concluded (page 72) that the “target zones” as I envisaged them would be characterized by

- soft margins, rather than a commitment to prevent the rate from straying outside the target zone;
- a zone perhaps 20 percent wide, outside of which rates would be considered “clearly wrong”;

1. Incidentally, I am not sure whether Fred or I should claim any credit for the volatility/misalignment distinction, which became quite popular around 1983. I decided that it would be counterproductive to draw attention to any role we might have had in propagating the distinction, which might merely have prompted the fanatical floaters into denying a distinction that had caught on naturally because it responded to a widespread concern.

- a crawling zone, with the crawl reflecting both differential inflation and any need for balance of payments adjustment;
- publication of the target zone; and
- the partial direction of monetary policy (perhaps in the form of intervention that is not fully sterilized) to discourage the exchange rate from straying outside its target zone.

Fred was never happy with my support for the first of those features, the soft margins. He argued that speculators would be less inclined to enter the market in a stabilizing direction if they knew that the authorities had reserved the right to let the rate go outside any target zone. My reply was that the authorities were not in a position to guarantee that under no circumstances would they let rates deviate beyond the target zones they had named: The costs might simply be too great. He doubted that, because he always had more faith than I did in the power of intervention. (I eventually thought I had found a solution, which was to make fiscal policy a systematic part of the policy prescription, but he didn't like that either, as I will shortly recall.)

Fred had no difficulty with my suggestion that bands should be something like 20 percent wide. The remark about rates being "clearly wrong" outside the target zone was an attempt to respond to German critics like the late great Otmar Emminger, who had a habit of saying that while he had no idea what the right rate was he could certainly recognize a wrong rate. Well, I would say, tell me your wrong rate, then imagine that the problem is too weak/strong a currency rather than too strong/weak a currency, and tell me what the wrong rate is on that side too. I guessed that those rates would turn out to be about 20 percent apart, so this would give you a target zone. I fear I didn't persuade him!

The crawl feature was of course a carryover from what I had long argued: There is no point in abandoning a proposal just because it is old; the more relevant question is whether it is right. I thought of a crawl as being satisfied by a series of small steps, as a number of member countries were at that time organizing their European Monetary System (EMS) realignments.

I was always an emphatic supporter of publication. I could never understand how officials believed that transparency could harm them, but many did. On the other hand, while Fred also would prefer publication, he tended to see this as an area where one could compromise. If officialdom felt more comfortable with target zones that they kept secret, so be it.

I argued that the prime policy instrument used to defend target zones should be intervention, a part of which should be unsterilized. (At that time we were still recovering from a decade dominated in our field by the monetary approach to the balance of payments!) Fred had reservations regarding the idea that intervention should be left partially unsterilized, re-

flecting his greater optimism concerning the effectiveness of sterilized intervention. I did not categorically rule out other instruments, notably capital controls, but neither did I express enthusiasm for them.

Fred has argued that the greatest influence of the Institute on exchange rate policy arose in the subsequent period, on the basis of the unvarnished target zone proposal. The Plaza Agreement marked the return of the Reagan administration to concern about exchange rates. Several months before this the number two official in the Baker Treasury, Richard Darman, had lunch with several Institute scholars (Fred Bergsten, Stephen Marris, and me) to talk about how we envisaged a target zone system working. In due course the US Treasury decided that the dollar had fallen enough and needed to be stabilized, which led to the Louvre Agreement. This agreement can be regarded as endorsing some sort of target zones, although there are many important divergences from the proposals I had previously laid out. For example, there was no provision for a crawl to offset inflation differentials, *target zones* were called *reference ranges* and were defined in terms of dollar rates rather than effective rates, the ranges were provisional “until further notice” rather than containing provisions as to how they should be altered, they were unpublished but in fact centered on the rates prevailing on the date of the agreement, and they were much narrower. Their narrow width may explain why they had to be ditched unceremoniously after the stock market crash in late 1987. Perhaps the most important, though least obvious, difference is the fact that while policies leaned more heavily against exchange rate changes as long as they did not exceed 5 percent from the target, pressure was eased when the market rate deviated more from the center of the range. According to Funabashi (1988, 185), beyond 5 percent “the only obligation was consultation on policy adjustment and realignment.”

While my own later work eschewed the terminology and has recognized some of the critical arguments, Fred has remained an unapologetic advocate of unvarnished target zones (Bergsten 1988, 1993, 1994, 1995; Bergsten and Henning 1996). In several respects those papers incorporated proposals articulated above, such as the size of the ranges and the means of determining their central rates, public announcement, frequent reappraisal of the appropriateness of the real zones, a crawl to offset inflation differentials, and a commitment to concerted intervention to defend the zones. Fred’s 1993 and 1995 papers both suggested that the world had tried fixed rates, under Bretton Woods, and floating rates, during the subsequent nonsystem, and was now moving toward an intermediate regime. His 1995 paper also had a graphic depiction of how the dollar overvaluation of the first Reagan administration had nurtured protectionism that was still haunting the world (in particular, in the form of Super 301).

His article with Randy Henning also makes two major points that seem to me questionable. First, they argued that target zones should really be viewed as a variant of flexible rather than fixed exchange rates. Clearly

the authors are right to argue that target zones are a form of intermediate regime rather than either extreme, but if one has to identify a cut-off between fixed and flexible rates, then my choice would be to ask whether at some rate there is a legal obligation to intervene to defend a margin, and on that test, target zones (at least with hard margins) are a form of fixed-rate system. More fundamentally, Fred and Randy attacked the consensus critique of policy coordination, which argues that monetary policy is already preempted by pursuit of the optimal combination of inflation and unemployment and therefore leaves no room to pursue an external target as well. They asserted that one will usually get a better *domestic* outcome by factoring *external* considerations into the decision. Logic says that it is not possible to improve on something that is already optimal, so the claim must be that the attempt to pursue what is domestically optimal is empirically prone to be inferior to the result achieved by looking at exchange rates. They give some telling examples, like US monetary policy in both the early and the late 1970s. Perhaps one could add current events in New Zealand as another instance where ignoring the external situation has led to an outcome that is distinctly suboptimal. So they may be right, but I confess that I am not yet persuaded of the general truth of this claim.

Be that as it may, it is surely not such considerations that have disappointed Fred's hopes of the early 1990s that the world was moving toward an intermediate regime based on target zones. On the contrary, the subsequent period witnessed the emergence of the "bipolar doctrine" (the notion that feasible exchange rate regimes are the two extremes, rigid fixity and free floating, and that all intermediate regimes are crisis prone and therefore undesirable). What are the reasons for the lack of appeal of anything like target zones?

The most important is probably the apparent difficulty that the world has in agreeing what equilibrium exchange rates are. Even in what seem to many of us to be absolutely unambiguous cases, like the renminbi peg, one finds economists with Nobel prizes and others paid inordinate sums by investment banks and at least part of the IMF staff prepared to assert that they do not know whether the renminbi is undervalued or not. If one then tries to take the analysis back a step, to search for exchange rates that will achieve an agreed set of current account targets, one finds that it is similarly impossible to secure agreement on what current account targets should be. Unless and until this sort of intellectual *laissez-faire* leads to the world ending up in a new depression, it seems hopeless to imagine that it can be changed.

A second important reason for the lack of support for target zones is the widespread belief in evidence of the absence of Krugmanesque stabilizing speculation (Krugman 1991) induced by such zones. To some of us the most important result is still the finding that the European Exchange Rate Mechanism (ERM) created a market expectation that the exchange rate would revert toward the center of the band (Svensson 1992). But Svens-

son's other findings, that Krugman's assumptions of perfect credibility and no intramarginal interventions are overwhelmingly rejected by the data, seem to have led to a general belief that zones have no stabilizing effect. Of course, no one doubts that a *credible* target zone would be stabilizing: The problem is that most target zones have apparently not been regarded as completely credible. After the ERM crises of 1992–93, or indeed the description of the reference ranges agreed at the Louvre as laid out above, it is not difficult to understand why. The world will clearly need to do better if it ever adopts a target zone regime.

A third reason cited by some is that inflation targeting seems to be proving a better basis for monetary policy than following an exchange rate target. This objection may not seem compelling to those of us who look to target zones to restrain markets from getting carried away on temporary errant paths, but there are still many economists who are unable to comprehend the possibility of misalignments and regard the only possible rationale for a fixed exchange rate as being to provide a guide for monetary policy.

The Blueprint

The next major development at the Institute on the question of managing the world economy, and the exchange rate regime that would facilitate this, was the "blueprint" for policy coordination (Williamson and Miller 1987), proposing rules for the coordination of fiscal and monetary policies among the G-7 countries. Monetary policy (interpreted as the short-term interest rate) was to be used to keep exchange rates within target zones around their FEERs, estimated as real effective exchange rates, as in the target zone proposal. The charge of critics that such a use of monetary policy might destabilize domestic demand was countered by introducing Keynesian fiscal policy. If, for example, an expansionary monetary policy designed to depreciate the domestic currency had an unwelcome by-product in expanding demand and thus stimulating inflation, then the answer posited was to tighten fiscal policy. Conversely, the implications for domestic demand of a tight monetary policy could be countered by an expansionary fiscal policy.

Since exchange rates are influenced by interest *differentials*, the proposed assignment left the world *average* interest rate indeterminate. (This is the old $n-1$ problem.) We argued that a symmetrical world system would provide that such a world variable should be determined by the needs of the world economy as a whole, rather than the needs of a particular country (as a dollar standard provides). In particular, we suggested that the world level of policy interest rates should be raised when the world was in a dangerously strong boom and lowered during a world recession. Concertation of such movements would be a responsibility of the G-7.

The other element of the blueprint was a proposal to vary fiscal policy in order to maintain “internal balance,” which was defined in terms of a growth rate of domestic demand that would “promote the fastest growth of output consistent with a gradual reduction of inflation to an acceptable level and agreed adjustment of the balance of payments” (Williamson and Miller 1987, 2). The desired nominal demand growth was to be determined by something that looked rather like a Taylor Rule, and fiscal policy was then to be varied in the short-run manner advocated by the OECD in the 1960s in order to keep demand on track, given the interest rates that materialized jointly from world decisions and the need to keep the exchange rate within its target zone. Fred was highly skeptical of this approach, because he never thought the Congress would abandon its sovereign right to change taxes and expenditures without regard to the rest of the world.

Be that as it may, the blueprint created a lot of interest in the academic world (as opposed to the official community, which treated it with the same reservations as Fred). For the next several years I wrote a number of papers that elaborated on various aspects of the proposal and even found myself having to defend what became known as the “orthodox assignment” (monetary policy to the exchange rate and fiscal policy to internal demand) against proponents of the “heterodox assignment” (fiscal policy to manage the balance of payments and monetary policy to internal demand). Randy Henning and I wrote a paper that tried to explore the political economy implications of implementing the blueprint for the Institute conference that celebrated the 50th anniversary of the Bretton Woods conference (chapter 2 in Kenen 1994). We were vigorously attacked by Richard Cooper in his capacity as one of our discussants at the conference, on the grounds that, first, calculating the FEERs required as input a set of targets for current account balances and no one could agree what targets are appropriate and, second, that subjecting fiscal policy to supranational constraints is inconsistent with democracy.

Intervention

As already noted, one way in which Fred and I have disagreed over the years is in the power we attach to sterilized intervention in the foreign exchange market. The Institute’s most impressive contribution to this perennial debate was the publication of *Does Foreign Exchange Intervention Work?* (Dominguez and Frankel 1993). In this work, the authors used previously unavailable daily data from the Fed and the Bundesbank to examine the effects of their sterilized purchases and sales of each other’s currency for their own in the 1980s. They combined these data with foreign exchange rates, press reports of intervention, and surveys of foreign

exchange traders about their expectations of future exchange rates and reached the following conclusions:

- Foreign exchange intervention can be an effective tool in influencing exchange rates, even when it is sterilized.
- Intervention is more effective when it is publicly known.
- Intervention may well work through some channel other than the traditional “signaling channel” (in which the central bank uses intervention to signal future changes in monetary policy) and “portfolio-balance channel” (in which it changes the relative supply of imperfectly substitutable bonds). In particular, it may work by pricking a speculative bubble. This is consistent with the greater effectiveness of publicly known intervention.
- They endorsed the previous finding that coordinated intervention is more effective than unilateral intervention.

At almost the same time, a conference in honor of Rinaldo Ossola heard a paper by three Banca d’Italia economists (Catte, Galli, and Rebecchini 1994) who also had access to daily data on intervention and also came to the conclusion that intervention had been an effective tool. They claimed that in about half of the 19 instances of intervention they identified, the course of the dollar had been definitively reversed, while in the other half the impact appeared to have been temporary. Discussants quibbled about whether some of the “definitive reversals” were really so definitive and whether many of the “temporary reversals” marked much of a reversal at all, but the general impression left by both this paper and the Dominguez-Frankel study was that sterilized intervention had been reinstated as a policy tool. However, both papers leave it open for Fred and me to maintain our individual views about whether intervention is a reliable tool that can be used in all circumstances and with reasonable assurance that it will work.

In a recent conference volume edited by Fred and me (Bergsten and Williamson 2004), two interesting papers reinforced themes that have been emerging in recent years. Chris Kubelec argued (and presented empirical evidence to support the thesis) that intervention was far more likely to be successful if it was attempting to reverse a large misalignment (which is consistent with the Dominguez-Frankel hypothesis that it may be particularly potent if it pricks a speculative bubble). In the other paper, Marcel Fratzscher treated intervention as not one but two policy instruments, one being trading in the foreign exchange market and the other “oral intervention” (a.k.a. jawboning). The fact that he finds a significant effect of oral intervention reinforces the suggestion that intervention should always be publicly announced.

Crawling Bands for Emerging Markets

In the 1990s the battle to persuade the G-7 countries to adopt more ordered exchange rate arrangements was lost. On the other hand, several emerging markets had adopted the sort of exchange rate arrangements that could have been described as target zones. But by then Paul Krugman had appropriated the term “target zone” to refer to the constant-nominal-rate bands of the EMS. Jacob Frenkel, soon after his appointment in 1991 as governor of the Bank of Israel, saved the day: He announced that the Israeli band would in future crawl according to the preprogrammed rate of deceleration of inflation, and that Israel’s new system would be called a “crawling band.” Hence (at least to some of us) target zones became crawling bands.

The two principal Institute publications that dealt with crawling bands were both by me (Williamson 1996, 2000). The first of these examined the operation of crawling bands in the three emerging markets that had the longest and most extensive experience with the regime and were still using it in the mid-1990s: Chile, Colombia, and Israel. In the event, in years subsequent to the book’s publication, all three countries allowed their exchange rates to float. It is notable that in all three cases the shift to floating went rather smoothly: It was demonstrably less traumatic than in the many other countries that started to float in response to a crisis. If the role of the crawling band is only to enable countries to learn to float, it will still have served a worthwhile historical function.

The other of my two books was written after I emerged from my three years at the World Bank, as a response to the so-called bipolar thesis that became popular among economists after the Asian crisis. According to this thesis, the growth of capital mobility had narrowed the options for exchange rate policy to a choice between freely floating exchange rates and rates that were permanently and credibly fixed. (When the thesis was first expounded, there was an unfortunate tendency to take Argentina as the example par excellence of the second case; after the Argentinean implosion, it was quickly decided that Argentina had not had a real currency board and had therefore not deserved its star position.) My counterarguments were:

- There are other objectives besides avoiding crises, which may also be important for welfare, like avoiding excessively overvalued exchange rates.
- Even corner regimes may be subject to crisis (an argument that suddenly became more convincing the next year when Argentina abandoned its fixed rate in the midst of a horrendous crisis).
- There is nothing in the Impossible Trinity analysis that prevents countries from choosing an intermediate position, e.g., with limited capital

controls, efforts to influence the exchange rate, and limited freedom for monetary policy. (An analysis of the Chilean experience with capital controls in the 1990s argued that there were serious defects in the literature that had dismissed their effectiveness.)

- Even if countries might hesitate to commit themselves to defend an exchange rate target, they could usefully adopt a reference rate.

But that is a topic best discussed a little later.

Baskets

Under strong pressure from Fred to contribute to thinking about the problems of a part of the world that he perceived as critically important to the United States, I became interested in exchange rate policies in East Asia. Initially the interest focused on the policies of the newly industrialized countries, or NICs (as they were then called), especially Korea and Taiwan. Bela Balassa and I wrote a Policy Analysis that concluded that the NICs needed to revalue, and expand demand, as a contribution to the adjustment process (Balassa and Williamson 1987, revised edition 1990). This may have contributed to the decision of the US Treasury to cite them for currency manipulation. The current account surplus decreased notably in 1989, and in the second edition we argued—to the annoyance of the US Treasury—that both Korea and Taiwan (but not Singapore) had done enough to justify dropping the manipulation charge.

Shortly before I went on leave to the World Bank in 1996, Fred again urged me to address the currency issues of the region, this time more generally. I could see little logic in the fact that most of those economies² pegged their currencies to the US dollar as though we still lived in the 1960s. True, this had the advantage of avoiding intraregional exchange rate changes, but that could equally well be achieved by having them all peg to any other unit, as long as it was the same unit for all of them. In particular, it seemed natural to explore the conjecture that they would be better served by pegging to a common basket of currencies that reflected the average trade weights of the group.

Hence I endeavored to make a comparison of the merits of a dollar peg versus a common basket peg for a number of East Asian currencies. In the version of the paper that was presented to a conference in Seoul in November 1996 and in due course published (Williamson in Collignon, Pisani-Ferry, and Park 1999), I argued that at least six and possibly as many as nine East Asian currencies should peg to the same basket. The six

2. When on one occasion I carelessly wrote “countries” instead of “economies” in a paper presented in Beijing, I was chided by a student on the grounds that Hong Kong and Taiwan are not countries.

core members of the group, identified by the similarity in their trading patterns, were China, Hong Kong, South Korea, Malaysia, Taiwan, and Thailand. Both the Philippines and Singapore were marginal on one of my two criteria, while Indonesia was marginal on both³, so I offered five comparisons. These involved actual policy; a unilateral peg to a basket of currencies with weights reflecting national trade patterns; a peg to a basket with weights reflecting the total trade of all nine economies; and similar baskets with weights reflecting the trade of eight and six economies, respectively. I showed that about 85 percent of the potential benefit of reducing instability of the nominal effective exchange rate to zero through using a unilateral basket peg could have been realized through (any of the) common basket pegs.

One of the issues that Fred wanted me to return to after I left the World Bank in 1999 was that of East Asian exchange rates. By now, after the East Asian crisis, a majority of the countries were nominally floating rather than pegging. In Williamson (2005), which appeared shortly after the much vaunted but de facto minimal change in Chinese policy in July 2005, I therefore referred to using a currency basket as the numeraire, a phrase sufficiently general to encompass not only a peg but also the measure of currency strength with reference to which authorities with a floating currency might intervene. A switch to a basket numeraire would still have the same basic effect of reducing instability of the effective exchange rate while avoiding any potential loss of competitiveness against other East Asian countries. And it would have resolved the collective action problem that seems to be a major factor explaining the fact that most of East Asia rode the dollar down when the dollar correction finally started in 2002.

The idea of pegging to a basket for countries with diversified trade had long been a part of my policy recommendations for emerging markets (at least since I surveyed the literature on the optimal peg, in Williamson 1982). I emphasized in my 1996 Policy Analysis that both Chile and Israel pegged (at that time) to baskets. But it was only after the East Asian analysis was developed, in 1996, that baskets achieved parity of esteem with bands and the crawl. It was then that Dornbusch and Park (in Collignon, Pisani-Ferry, and Park 1999) first referred to my proposals as the BBC system (basket, band, and crawl).

The System: Tinkering or Reference Rates?

For many years the Institute's monetary economists were effectively Fred Bergsten and me. Bill Cline did some valuable studies on debt and adjustment, and Steve Marris was here for a while, but I think it is fair to say

3. One criterion involved similarity in the geographical distribution of trade and the other that the countries be close competitors in world markets. Singapore was marginal on the first criterion and the Philippines on the second.

that we were the core staff interested in exchange rate regimes. That changed with the appointment of Morris Goldstein as a senior fellow in 1994. Since then it has changed even more dramatically as we have been joined by Martin Baily, Catherine Mann, Mike Mussa, Adam Posen, and Ted Truman. The new appointments have a distinctly less positive attitude toward attempts to redesign the global monetary system of the sort that have always appealed to Fred and me and are more inclined to search for modifications of present arrangements.

The future trend was trumpeted in the subtitle of Morris Goldstein's first publication for the Institute (Goldstein 1995): "A Modest Agenda." (No one remembers what the main title was, but everyone remembers that the Institute actually suggested something modest.) He proposed accepting the main features of the existing international monetary system but emphasizing the avoidance of large misalignments and having the main countries shift monetary policy away from purely domestic concerns in the event of a large misalignment, although keeping estimates of equilibrium exchange rates secret ("quiet"). Other proposals involved the IMF taking a more active role in diagnosing misalignments and prescribing policy adjustments and having the main industrial countries accept that the IMF ought to play such a role. The Fund needed to improve the flow of information to the private capital market (this was before the Special Data Dissemination Standard was invented). It also needed to reexamine the concepts of "exchange rate manipulation" and "unfair competitive advantage" to try and make them operationally useful.

His subsequent Policy Analysis, *Managed Floating Plus* (Goldstein 2002), was if possible even more emphatic in advocating the preservation of floating exchange rates. Most of the manuscript was in fact about the "plus," which consisted of inflation targeting and an effort to avoid currency mismatches. It always seemed to me that the less satisfactory part of the paper was about managed floating, specifically that it did not advocate the management of floating in any sense that I would recognize the word "management." He wrote (page 43):

I call it "managed" floating to indicate that . . . the authorities could use various policies to counter some short-term movements in the exchange rate. They would be permitted . . . to intervene in the exchange market . . . to "smooth" what they regarded as excessive short-term fluctuations in exchange rates.

Later (page 44) he explains that the authorities would have no publicly announced exchange rate target and in a footnote emphasizes that, in contrast, most intermediate regimes do have a publicly announced target. This question of publication has increasingly struck me as the crux of the issue.

My own writing (e.g., Williamson 1998, 2006) has tended to accept that countries cannot be expected to commit themselves to defending any exchange rate target. In that sense, they float. However, the essence of man-

agement is that the authorities need to indicate when intervention is to be expected and to spell out their objectives and the criteria that could be used to judge their success. One possibility would be to announce a “leaning against the wind” strategy (Wonnacott 1958), but the objection to that is that it might oblige them to resist a change of which they approved (i.e., one that was tending to reduce a misalignment). If one thinks that misalignments are the problem, then the logical solution is to sanction intervention (or policies with the same objective) that would tend to reduce misalignments. That could be done either by prohibiting intervention (or other forms of management) that would tend to push the exchange rate away from a “reference rate,” or by prohibiting all intervention inside a “monitoring zone” as well as any intervention that would push the rate away from that zone. But in either event there would be a need to identify and publish a target rate (i.e., the reference rate or the center of the monitoring zone). Fred regards this as less likely to be acceptable to officialdom than target zones because it involves the adoption of point estimates of equilibrium rather than ranges. (One way of meeting this difficulty would be to adopt the monitoring zone variant of the proposal.) The virtues (and vices, if there are any, apart from the unworthy desires of officials not to be held accountable) of publication need to be discussed. That is an assignment for the future.

Concluding Remarks

It is clear that Fred and I have not persuaded officialdom, or the economics profession, or the public, or even all our colleagues, that unmanaged (as I define them) floating exchange rates are not the best possible arrangement. Even if that remains true, there is perhaps some value in having helped to propagate regimes that have enabled countries to learn to float and so transition to floating without a crisis. Or else there would be value in having aided East Asia to move toward a regime that resolves the collective action problem that has so far caused it to ride the dollar down whenever there appeared to be a possibility of sufficient dollar adjustment to head off global economic crisis. And if we have helped develop thoughts toward the form that a backup regime might take if and when the nonsystem enters crisis, this too might justify our efforts.

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