# The problem with ‘embedded liberalism’: the World Bank and the myth of Bretton Woods

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## *The problem with ‘embedded liberalism’: the World Bank and the myth of Bretton Woods*

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# The problem with 'embedded liberalism': t

The Bretton Woods conference is conventionally understood as a radical break between the *laissez faire* order and its 'embedded liberal' successor, in which finance was suppressed in the interest of trade and productive growth. The new institutions, particularly the IBRD are often considered emblematic of this. In response to this, the paper argues that the Bretton Woods order required the enlistment, not repression, of private American finance. Firstly, *laissez-faire* era proposals for international financial institutions provided important precedents for the Bretton Woods institutions. Second, these were predicated on the uniquely deep liquidity of American financial markets following upon Progressive-era reforms, in the legacy of which the Roosevelt administration sought to locate the New Deal. Thirdly, they found new relevance in the 1940s as the IBRD turned by necessity to American financial markets for operating capital. Negotiating the imperative of commercial creditworthiness had two important consequences. First, it entailed the structural and procedural transformation of the IBRD, and allowed management to carve out a proprietary terrain in which its agency was decisive. Second, this suggests that US agendas were mediated by the Bank's institutional imperatives – and that finance was no more 'embedded' during the Bretton Woods era than its prede-501]TJETBT/F4 11.04 Tf1 0C014ps(p)3(ro)-3W1 0 02r765.53han its

famously, Ruggie (1982) has argued that this agenda was institutionalised in a new 'embedded liberal' order.

The concept of 'embedded liberalism' has become a touchstone of our understanding of the Bretton Woods era. It is commonly suggested that an anti-financier agenda was clearly reflected in the fact that the negotiators at Bretton Woods were the representatives of states, while financiers were conspicuously absent (Kapur, Lewis, & Webb, 1997a: 906-7,912). As multilateral international organisations, the Bretton Woods institutions are conventionally considered to exemplify a decisive turn away from the practices of the inter-war period, when international financial and monetary planning was undertaken by private financiers on behalf of national governments. This is not only the case for accounts of the post-war regime – much of the literature which aims to historicise the later neoliberal turn in global governance is founded upon the notion that finance has been 'disembedded' from the apparatus through which the power of financiers was repressed in the Bretton Woods era.

Yet these accounts of the post-war international order rest on surprisingly little evidence. Their principal focus is upon the novel features of the post-war regime such as capital controls. This should not be taken to mean that the policy shifts which are identifiable in the monetary and financial policies of governments on both sides of the Atlantic are insignificant. But this emphasis on national regulations such as capital controls does not help us to understand the nature of the structures of governance at the international level. The key evidence which supports these accounts of the international order is, in terms of the precise mechanisms through which it was governed, essentially circumstantial.

It is not a co-incidence that one of the most striking features of accounts that rest upon the 'embedded liberalism' concept is the way in which the primary agent of the new consensus is often considered to be the IMF – precisely that agency with the remit to manage capital controls. It is clear enough that the planners of Bretton Woods considered that the Fund would play the most prominent role in negotiations aroun(c)3(h)-4( 1 72.024 231.06B

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rhetoric of the period, these accounts overlook the extent to which the Bretton Woods regime was shaped by the engagement as well as the opposition of financiers.

In this paper, I shift the focus away from national-level policy instruments and the intentions of policymakers to the specific mechanisms of international governance. I argue that an analytical focus on the IBRD allows a different reading of the governance of the post-war order. Through a revisionist history of its foundation I show that the capitalisation of the Bank via private American finance poses a substantial challenge to conventional accounts that claim that the post-war order was predicated upon the suppression of finance in a radical break with the *laissez-faire* era. Rather, the Bank should properly be located in the lineage of private financiers' plans for a multilateral organisation in the inter-war period. This suggests a greater degree of continuity across these periods than the radical break in practices which is conventionally assumed in the 'embedded liberalism' narrative.

Moreover, the broad principles concerning the operation of the new institutions rapidly proved too vague to direct practice concretely. Ultimately, private American capital markets were the only source from which the Bank could obtain operational capital in sufficient volume, and commercial creditworthiness became an institutional imperative. This does not imply exchanging US dominance for financiers' dominance of the institution. Negotiating this financial imperative successfully – getting the Bank up and running on a sustainable basis - would entail the pragmatic transformation of the managerial relationships and operating procedures with which the Bank had begun life. In the course of this process, the Bank's management was able to carve out a proprietary terrain in which their agency in setting policy and procedure was decisive – within the parameters set by the Bank's social anchoring in American finance.

The necessity of enlisting American finance in the operationalisation of the IBRD constituted an institutional legacy with profound long-term implications for the governance of the Bretton Woods regime. It is these critical institutional features of the post-war international order which are not captured by the 'embedded liberalism' narrative, which as a result provides a curiously impressionistic account of the infrastructure of governance which would come to define the era. Therefore, in what follows I explore the construction of the terrain of managerial agency in the Bank that enabled it to negotiate the imperative of commercial creditworthiness that constituted the parameters of its pursuit of US interests. I trace the development of this critical managerial capacity in three steps.

In the first section I review the existing literature which constitutes the 'embedded liberalism' narrative. I argue that the main problem with it is the circumstantial nature of the evidence upon which it rests. Further, by characterising the Bretton Woods regime as a decisive break with the practices of the inter-war period, it obscures the longer lineage of precedents for the Bretton Woods institutions which is to be found in the era of *laissez-faire* liberalism. The parameters within which a new international regime could be operationalised during the 1940s precluded a radical break with the material resources of private finance. Plans put forward by private financiers for multilateral international financial institutions during the 1920s constituted intellectual and pragmatic touchstones upon which the Bretton Woods planners would draw. This suggests that the demarcation of the two regimes is conventionally overdrawn.

In the second section I explore the relationship between the Bank and private American finance in the passage of the Bretton Woods Act. Wall Street's apparent opposition to the new institutions is a central feature of the 'embedded liberalism' narrative – yet this centred upon the Fund rather than the Bank. It was envisaged from the outset that the IBRD would have a close working relationship with private US capital, and it followed that of the two institutions it was the Bank which emerged the stronger from Congressional negotiations over the Act.

Finally, I show how the nuts-and-bolts of the roles and relationships of the institutions of post-war governance were worked out pragmatically in the course of the Bank's earliest operations as it turned, under pressure from the Truman administration to begin lending, to the US bond market for operating capital. Negotiating the institutional imperative of commercial creditworthiness this bequeathed would, I illustrate via a discussion of the transition from the management of President Meyer to President McCloy and the 1947 loan to Chile, shape the organisational structure, policies and practices of the Bank from the outset.

Ultimately, financiers' enlistment was essential for the successful operationalisation of the IBRD. This matters for our understanding of the post-war international economic regime because it illustrates that from the outset, far from repressing finance and embedding it anew in wider social purposes or subjecting it to public agendas, an infrastructural relationship existed which connected the Bank and private US finance at the heart of the Bretton Woods order.

## 1: A Break with Liberal Tradition in International Finance?

That the problems faced by the US in creating a new international order after WWII reflected those it had faced after WWI has been widely noted (Thorne 1978, Orde 1990), as has the dogged continuity of the American liberal political tradition by comparison to social-democratic trends in Europe (Rodgers 1998, Ruggie 1982: 405-6). These observations are complemented by a deeply-rooted narrative which mythologises the Bretton Woods order as an historic compromise which rested upon the willingness of the US to trade international capital mobility off against a liberal multilateral trading order.

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New Deal policymakers faced a similar dilemma to their Republican predecessors. Maintaining the stability of the currencies at the core of the global economy during the 1940s still, as in the 1920s, required the US to either increase the volume of goods imported from Europe and South America and sacrifice its own export surplus, or continue liquidity injections to Britain and Europe (Frieden, 1988). As the political cost of a balance of payments adjustment seemed too high, the latter strategy persisted – and inter-war proposals for a supra-national institution to mobilise the savings of the advanced industrial economies found new relevance.

That their salience often goes un-remarked is largely due to the emphasis the embedded liberalism thesis places on the ideological shifts of the 1930s and machinations over direct political access during the development of the institutional apparatus of the New Deal state. Financiers' proposals are conventionally understood as efforts to perpetuate the 'dis-embedding' of finance, as they were intended to support a gold-standard regime. By comparison, such narratives point out, the Bretton Woods negotiations were undertaken by civil servants and public intellectuals – bankers were not invited, and the objective was to promote public finance to a leadership role in international investment at the expense of private finance.

Yet the IBRD was initially conceptualised as a mediator between private financiers and member states, offering guarantees rather than lending on its own account. This should not be read as a significant departure from the visions of multilateral international financial organisations mooted by private financiers during the inter-war period. These may have failed to establish a new supra-national institution but their legacy may be seen in early conceptions

Three proposals made prior to the Dawes Plan by private financiers acting in quasi-official capacities are instructive in this regard. Two came at the 1920 League of Nations conference in Brussels. The first was the Delacroix plan. This proposed an international institution in which vision for the Bank, the conference envisaged that through the central institution, private finance would play a key role in investment -

## 2: Finance and Bretton Woods

In this section, I turn to the issue of financiers' relationship to the Bretton Woods proposals. Helleiner has argued that the Bretton Woods institutions were founded in spite of New York bankers' opposition (1994: 39-44). The official history of the Bank argues that

Morgenthau praised the Bank's role in support of finance – the IBRD would, by offering guarantees, complement private capital and facilitate the expansion of investment beyond its contemporary limits on a sounder basis than during the inter-war boom. This should be seen in the context of the effort to break the Morgan monopoly in the form of the 'money trust', to which he alluded in the same speech: *'Capital, like any other commodity, should be free from monopoly control, and available upon reasonable terms to those who will put it to use for the general welfare'* (United States Government, 1948: 1119).

It had been understood in financial circles for some time before the Bretton Woods conference that the future of the international monetary system would not look the same as the past. Behind the 1932 New Deal programme of financial regulation, expansionary domestic monetary policy, devaluation, and the protectionism of the National Recovery Administration stood industrialists, farmers, oil companies – and major anti-Morgan financial interests including newer firms pace, the shared interest of industry and finance in traditional liberal international political economy was disappearing.

For all that the Glass-Steagall act had altered the institutional makeup of the financial system and the new Securities and Exchange Commission policed the financial markets, financiers were integral to the social compact which supported the New Deal. As Martijn Konings has suggested, contrary to the embedded liberalism thesis, such instruments sought to harness, not to negate, the power of finance in the service of the New Deal as the inheritor of Progressive tradition (Konings, 2011).

The institutions under discussion at Bretton Woods did not represent an attempt to break with this compact. Rather, the IBRD in particular was conceived as an attempt to harness the unique capacity of the private US financial market to deliver the capital the international system required. It is in the context of financiers' support for the New Deal and against the longer background of the deepening social importance of finance that we should view the foundation of the Bretton Woods order, to which I now turn. Enlisting financiers' support would prove essential to the passage of the Bretton Woods Act through Congress.

## The passage of the Act through Congress in spite of financiers' opposition

revisions to the Act were proposed, on the basis of which it was concluded that the new institutions would co-operate with private financiers to facilitate flows of private portfolio investment where this would not occur under normal market conditions.

This was reflected in a January 1944 question-and-answer document shared with foreign representatives ahead of Bretton Woods – with strong echoes of the Delacroix and Ter Meulen Plans. Investment capital should be provided by private investment channels supported by Bank guarantees, and only supplemented through Bank participation in loans, or ‘encouraged’ through direct lending. From this point onwards, the Treasury’s concept of the Bank reflected financial concerns and aimed to encourage private capital to invest overseas by offering guarantees –

clients that had endured since the onset of the Depression, the Bank could play a major role in re-establishing profitable conditions for international investment.

On the other hand, they argued that the Fund should be deferred. Financiers' opposition took a familiar form – around the same arguments that had confounded the Delacroix and Ter Meulen plans: the contravention of national sovereignty, and potential to cause inflation. During the 1945 Congressional hearings, a loose coalition of isolationists, Republican business-people and laissez-faire conservatives began to coalesce around the argument that the Fund was little more than a trick by which governments would be allowed to avoid responsibility for enacting unpopular internal adjustments (Ferguson, 1984). This group, allied with prominent figures in the American financial community who had previously supported the Roosevelt administration, lined up in favour of supplanting the Fund with a stabilisation programme akin to the 19th century form of the gold standard (Eckes, 1975: 174).

Their alternative was formulated by John H. Williams, vice-president of the FRBNY. By stabilising the dollar and sterling, international trade and finance could be organised without any kind of international governing body. Re-opening the City of London as an international capital market could reduce the strain on the scarce dollar and facilitate European-US trade. To this end, Britain should be offered significant dollar funds in either credits or aid grants (Williams, 1943). The system simply needed enough capital.

The bankers' argument was sound. Britain was obliged under the IMF's Articles of Agreement to eliminate payments discriminations and return to multilateral convertibility, and desperately needed funds to stabilise sterling. Failing to provide this capital would, they noted, threaten the dollar-based blueprint for the post-war era: Parliament would have been unlikely to ratify the Act if faced with the prospect of competing for dollars with other Fund members.

A loan of $3.75bn and a $20bn write-off of wartime assistance followed this realisation – effectively instituting the core of the Williams Plan. Although these agreements failed to secure the multilateral convertibility of sterling, they reflected an unavoidable

Passing the Act required a further trade-off between the Roosevelt administration

## 3: Negotiating the Imperatives of American Finance: Operationalising the Bank.

In what remains of the paper, I argue that the process of making the Bank operational was directed most importantly by pragmatic concerns. The exigencies of capitalisation necessitated major organisational and procedural transformations, and in this way, the enlistment of private US finance in support of the IBRD created an institutional legacy of lasting significance for the governance of the international order.

Operations were intended to begin by the end of 1946: the Truman administration was eager to get the Bank up and running quickly. Even before the Point Four agenda, the ambitions of the US in this regard posed significant problems for the originally preferred model of the Bank as a guarantor linking private capital with willing borrowers. The IBRD direct lending operations originally envisaged. Worse, costs to borrowers may in any case have varied among applicants on the basis of their creditworthiness. Further, Daniel Crena

1945, they had begun a program of policy-formulation in the process of which they would meet formally as often as twice a week and confer informally on a daily basis. According to Kraske, they considered private financial management of exchange and financial markets during the inter-war period a miserable failure. Given the high price industrial economies had paid for this failure, the post-war world economy should be '*guided by international institutions that had to answer to the governments which created and sustained them*' (Kraske, Becker, Diamond, Galambos, 1996: 26).

Prior to the appointment of the first President, Eugene Meyer, they had, under the leadership of US director Emilio Collado, made the Bank's initial calls on members' capital and invested the funds it received in US Treasury bills, notes, and certificates. They had secured the requisite amendments investors that the Bank would be run on the basis of commercial, not political, considerations (Bird, 1992: 282-5).

This is not to say that the new management pursued the interests of financiers to the exclusion of the aims of the Bretton Woods settlement. Rather than a zero-sum conflict between US state and financiers, while the Bank was a site of contestation it was also a site of pragmatic accommodation between bankers and state officials. Further, it reflects the pragmatic working-out of a concrete politics of governance that reflected the social relationships of the New Deal in which the Bank was anchored.

## 4: Conclusion

It is somewhat misleading to conceptualise the transition between the inter-war and post-war international regimes as a radical break between *laissez-faire* and a novel 'embedded liberalism'. Juxtaposing these phenomena directs the critical gaze away from the key problematique of the essential illiquidity of the international system which spanned the 1920s and the 1940s, and leads accounts of the post-war regime to miss the central role of the IBRD in the construction of the post-war regime. Further, by beginning with the New Deal and the transformative moment of the Bretton Woods conference, such accounts make significant assumptions about the capacity of the US to enact its strategies. Although the New Deal and Bretton Woods institutions were new ‘blueprint’ for the Bank was provided by financial planners of the *laissez-faire* era, and was borne out to a striking degree in the extent to which the new settlement ultimately rested upon private finance. As I have illustrated, in the 1940s, while financiers were displaced from the quasi-official roles they had held during the international conferences of the 1920s and in the development of the Dawes plan; it was neither possible nor strategically desirable for the New Deal administration to negate the social importance of finance. Drawing upon the deep reserves of liquidity created by mass participation in financial relations was explicitly envisaged from the outset.

The only question was how. The nuts and bolts of the new international order were not worked out at Bretton Woods. The specifics of the way in which the Bank would act to facilitate re-inflation of the international economy remained to be worked out after the first the ideology and power of its most important donor. Rather the way in which the institution was organised and the strategies it deployed to address US objectives were derived from management's pragmatic negotiation of the parameters set by its social basis in private American finance, as may be seen in the Chilean case.

Following from this, I suggest that reconceptualising the relationship between financiers and the Bretton Woods regime, and the key role of the Bank within it invites reconsideration of certain key features of literature on the international financial institutions in the governance of the post-war international order.

Primarily, it encourages us to rethink the oft-imagined consonance between the 'embedded liberal' regime and the 'development' agenda pursued by the Bank in apparent support of the Point Four programme during the Bretton Woods era. If the Bank depended upon the confidence of the hard-nosed financiers of Wall Street, how are we to understand the elaboration of a 'development' agenda?

The tentative sketch of the longer and surprising history of the Bank and its relationship to the uniquely deeply socially-penetrating financial infrastructure of the US which I have provided in this paper may provide an analytical starting point from which to begin to address these questions. I propose that we must carefully think through the implications of the Bank's social basis in American private finance, which I have begun to illustrate here. Financiers did not dominate the Bank, neither did state bureaucrats: managerial agency would become decisive in designing technologies of institutional governance and lending which allowed the Bank to solve its perennial problem of capitalisation within parameters defined by its social anchoring in US finance. Therefore, in addressing these questions with a view to intervening further in this crowded field, we must take the problematic of capitalisation as a starting point for understanding the emergence of the pragmatic agency of Bank management and its significance for the governance of the global political economy, from the post-war to the contemporary era.

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