Negotiating Credibility: Britain and the International Monetary Fund, 1956–1976

BEN CLIFT AND JIM TOMLINSON

Abstract

For twenty years before the famous crisis of 1976 Britain was a regular borrower from the International Monetary Fund (IMF). Through this lending role, the Fund in these years played a key part in determining the credibility of British policies. Borrowing from the Fund meant that British policy had to be seen as conforming to certain norms, but these norms were always negotiable, albeit within shifting limits. This article uses archival material from London and Washington to examine these processes of negotiation, showing how far British policy was shaped by the desires of the IMF, and how far it was able to maintain autonomy in national economic policy.

Along with other West European countries, Britain in the 1950s and 1960s pursued ambitious domestic policy objectives, especially full employment and fast economic growth, in an increasingly 'liberal' international economic environment. Although progress on this road was uneven, liberalisation of trade and capital flows increasingly exposed all these national economies to the possibility of increased international constraints on domestic policies.[1] Conducting such policies in this environment required that the authorities continually kept in mind the impact of domestic decisions on international opinion, especially the opinion of those who played a key role in decision-making in the major international economic bodies. Until the 1970s the most important of these bodies were the General Agreement on

Dr Ben Clift, Department of Politics and International Relations, University of Warwick, Coventry, CV4 7AL; B.M.Clift@warwick.ac.uk. Professor Jim Tomlinson, School of Humanities, University of Dundee, Dundee, DD14HN; j.d.tomlinson@dundee.ac.uk. The authors would like to thank the Carnegie Trust for the Universities of Scotland for financial support, and the ESRC-funded Centre for the Study of Globalisation and Regionalisation at the University of Warwick for funding Ben Clift's teaching buy-out which enabled parts of this research to be pursued. We would also like to thank the Department of Politics and International Studies at the University of Warwick for granting the study leave and providing the financial support which enabled the fieldwork in Washington to be carried out.

[1] S. Newton, *The Global Economy 1944–2000: The Limits of Ideology* (London: Arnold, 2004).

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Tariffs and Trade (GATT) and the International Monetary Fund (IMF). On GATT we may say that in broad terms this body's agenda of trade liberalisation, which Britain, of course, had helped to formulate, did not act as a major constraint on Britain's policies, which embodied a somewhat hesitant but persistent path to freer trade.[2]

In the case of the IMF, its role was crucial in these years, because it was not only the key international agency in regulating international financial policy, but also the provider of large amounts of finance for national governments and thus, as the body 'paying the piper', potentially able to 'call the tune'. (Later, from the 1970s, the role of the IMF was to diminish as private finance played a much larger role in international finance.[3]) The IMF's role in the context of the development of the international financial system has led to an enormous literature.[4] Much less systematic attention has been paid to the relationship between the IMF and particular national governments, although some texts do deal with elements of this story.[5] We may helpfully think of this IMF–national government relationship as concerned with the issue of how such governments could sustain credibility with the IMF, a credibility necessary if loans were to be obtained. This issue of credibility is at the core of the discussion of the crisis surrounding Britain's much analysed borrowing from the IMF in 1976.

Despite the mythology to the contrary, the IMF visit and subsequent loan was not the cause of the reversal of British economic policy seen in the mid -1970s. Rather, policy had already shifted fundamentally towards deflation rather than maintaining employment before IMF officials set foot in Britain.[6] This does not mean that the IMF was irrelevant to resolving the economic crisis of the time. The key role of the Fund was to give its seal of approval to British policy in order to rebuild confidence. As Burk and Cairncross put it, what 'financial markets . . . looked for was the acceptance by the IMF that enough had been done. Nothing less would have restored confidence in sterling.'[7] What was negotiated in 1976 was a 'stamp of approval' that restored the international credibility of British policy, ending the outflow of capital and the downward pressure on the exchange rate. The Labour government restored

2 R. Toye, 'The Attlee Government, the Imperial Preference System and the Creation of the GATT', *English Historical Review*, 118 (2003), 912–39.

3 R. Germain, *The International Organization of Credit* (Cambridge: Cambridge University Press, 1997).

4 The best short summary is B. Eichengreen, *Globalizing Capital: A History of the International Monetary System* (Princeton: Princeton University Press, 1996), ch. 4. Much more detailed are K. Horsefield, *The International Monetary Fund 1945–65: Twenty Years of International Monetary Co-operation* (Washington, DC: IMF, 1969); M. de Vries, *The International Monetary Fund 1966–1971: The System under Stress*, 2 vols (Washington, DC: IMF, 1976); M. de Vries, *The International Monetary Fund, 1972–78: Co-operation on Trial* (Washington, DC: IMF, 1985); H. James, *International Monetary Co-operation since Bretton Woods* (Washington, DC: IMF, 1996).

5 R. Solomon, *The International Monetary System, 1945–1976: An Insider's View* (New York: Harper & Row, 1977), ch. 5.

6 S. Ludlam, 'The Gnomes of Washington: Four Myths of the 1976 IMF Crisis', *Political Studies*, Xl (1992), 713–27.

7 K. Burk and A. Cairncross, *Goodbye Great Britain: The 1976 IMF Crisis* (New Haven: Yale University Press), 225.

credibility to its policy stance, exactly as a later generation of analysts would argue was the essential prerequisite to pursuing an independent national policy.[8]

But was the 1976 episode typical of the experience of the previous decades? As Britain pursued its domestic goals in a world of growing international capital mobility, combined with fixed exchange rates down to 1972, how far and under what conditions did the IMF act to provide the credibility which allowed national governments space to pursue such policies?

The process of negotiating credibility was highly political, focusing not only on specific policy measures but also on the major question of how far national governments could and should accept limits on their sovereignty. In 1976 this question was crucial to the domestic political dispute, polemicists claiming that acceptance of the IMF package was a humiliation in which Britain had lost the capacity to determine its own policies.[9] But whilst this argument took dramatic form in the mid-1970s, it was present, with varying degrees of prominence in British–IMF relations over the previous two decades. Alongside the issue of 'external' financial credibility was the need for any deal to have domestic political credibility.

Using archives in both London and Washington, this article places the credibility issue in the context of Britain's dealings with the IMF over the twenty years to 1976. In that period the British government was discussing the state of the British economy with the IMF for much of the time, either because of the frequent borrowings (standby arrangements) or through routine discussions. Before 1976, borrowing had taken place in 1956, 1961, 1962, 1967, 1969 and 1974–5, but such borrowings had to be renewed annually, and were thus subject to further negotiation.[10] Parallel consultative discussions took place under Article XIV and later Article VIII of the Fund Agreements.

Britain's dealings with the IMF in 1976 have been much discussed,[11] and there is also material on the 1967 devaluation and its aftermath.[12] We also have scholarly accounts of Britain's broader relations with the IMF, especially the role of sterling.[13] But we lack a long-term, analytic overview of Britain's relationship with the IMF over these two decades which draws together the experience of the whole period, focusing attention on the credibility issue and the interwoven question of the capacity

[8] E. Balls, 'Open Macroeconomics in an Open Economy', *Scottish Journal of Political Economy*, 45 (1998), 113–32. B. Clift and J. Tomlinson, 'Credible Keynesianism? New Labour Macroeconomic Policy and the Political Economy of Coarse Tuning', *British Journal of Political Science*, 37 (2007), 47–69.

[9] K. Hickson, *The IMF Crisis of 1976 and British Politics* (London: Tauris, 2005), chs. 4, 5.

[10] S. Gold, *The Standby Arrangements of the IMF* (Washington, DC: IMF, 1970), 210; de Vries, *International Monetary Fund 1966–1971*, 395–6.

[11] Burk and Cairncross, *Goodbye*; M. Harmon, *The British Labour Government and the 1976 IMF Crisis* (London: Palgrave, 1997); Hickson, *IMF Crisis*; de Vries, *International Monetary Fund 1972–78* ; M. Crawford, 'High-Conditionality Lending: the UK Case', in J. Williamson, ed., *IMF Conditionality* (Washington, DC: Institute for International Economics, 1985).

[12] De Vries, *IMF 1966–1971*, chs. 18, 21; Harmon, *British Labour Government*, 29–45; S. Strange, ed., *International Economic Relations of the Western World, Volume 2 International Monetary Relations* (Oxford: Oxford University Press, 1976), 135–72.

[13] E.g. S. Strange, *Sterling and British Policy* (Oxford: Oxford University Press, 1971); C. Schenk, *Britain and the Sterling Area* (London: Routledge,1994); Strange, *International Economic Relations.*

of national governments to determine their own policies, and it is to this analysis that this article contributes.

I

At the Bretton Woods negotiations the attitudes of a debtor country such as Britain and the world's major creditor, the United States, were bound to differ, and the difference was evident in the discussion of conditionality. Keynes, Britain's key negotiator at Bretton Woods, and the British wanted close to automatic access to the Fund's resources, the Americans substantial conditionality, in order to keep debtors in check. The US viewpoint was not embodied in the original Agreements but was introduced and developed through the 1950s, so that increasing emphasis on conditionality reflected the dominance of the United States within the organisation. In 1952 the standby arrangement became the standard form of IMF borrowing, providing a borrowing facility with increasingly tough conditions attached as the amount borrowed increased.[14]

Britain borrowed unconditionally from the Fund in 1947 and 1948.[15] Frequent borrowing began from 1956, when conditionality was already being applied to developing countries (the main borrowers in the period up to the late 1950s) but not yet to developed countries. Thereafter, conditionality in general increased, and over the next twenty years became more sophisticated and more substantial. This was the environment within which successive British governments had to work. Conditionality became markedly more exacting from the mid-1960s, the Labour government's period in office being accompanied by a significant shift in relations with the IMF. Standby arrangements between 1964 and 1969 saw a steady ramping up of the specificity of undertakings, performance targets and strings attached to borrowing on the part of an increasingly interventionist Fund. This is most clearly demonstrated with the increased frequency and formalisation of 'review' visits tied to standby arrangements, as in 1967 and 1969. There was concern on the IMF side of impartiality of treatment, given the (legitimate) grievance of other countries that the United Kingdom was getting too easy a ride in comparative terms. In 1968 the IMF regularised its standby arrangement procedures so that, formally at least, all borrowers receive equal treatment,[16] but IMF officials clashed over how this should affect IMF–UK relations. A consensus emerged to seek 'uniformity in spirit' if not uniformity 'in detail of form', effectively conceding less conditionality for the United Kingdom, justified because 'to a considerable degree, through the periodic review, we have in fact maintained a surveillance approaching that of other countries'.[17] There was a further evolution in 1973, as the IMF tried to recast its role of stewardship of the international monetary order. The Fund introduced a lighter-touch regime – a

[14] Gold, *Standby*.
[15] Horsefield, *International Monetary Fund 1945–65,* 464–7.
[16] IMF Archives (hereafter IMF), Staff Memoranda (hereafter SM), 68/128.
[17] IMF, UK Country files, 1760, Box # 32, File # 5, David Finch to the Managing Director 'United Kingdom Consultation under standby arrangement', 16 July 1968.

more informal approach to its interim consultations with those countries 'whose exchange rate policies have a major impact on the international monetary system'.[18] This heralded a shift to informal 'mini-consultations' for those routine interactions not tied to a standby arrangement.[19]

UK–IMF interactions were a 'repeated game' in the two decades under scrutiny, both sides learning from past interactions. UK politicians and officials became very familiar with IMF preferences and opinions in relation to particular policies. This 'feedback loop' makes it difficult to discern the precise degree of influence of the Fund; 'we knew what policies would be acceptable to [the Fund]; and when framing our policies we knew that we wished to make a drawing from the Fund. In these circumstances the distinction is a little subtle between submitting our policies for the Fund's approval and choosing policies we knew the Fund would approve.'[20]

The recurrent themes across the two decades was the balance of payments position, followed in importance by public expenditure growth. From the mid 1960s the Fund was increasingly anxious to introduce credit ceilings and some quantitative measure or target for monetary aggregates. As regards Letters of Intent which accompanied standby arrangements, from the mid 1960s onwards there was an increased emphasis on inserting trigger clauses, more precise performance criteria and quantitative targets to increase the specificity of government undertakings. In response, government officials began to pre-empt and seek to avoid being tied down to such targets and criteria. Towards the end of the period, when UK officials were preparing for an IMF borrowing in late 1973, much attention was paid to the 'preoccupations of the management and the partners', focusing on domestic credit expansion, taxation and the sterling rate as 'obvious candidates'. Policymakers considered 'the implications of accepting DCE (Domestic Credit Expansion) targets' (the IMF's favoured credit ceiling yardstick) and 'the arguments to be deployed if such proposals are made to us'. Treasury officials began both 'to list policies and measures already determined and announced which would make a good showing in a Letter of Intent' and 'to consider what other measures and policies the IMF (or European partners as a condition of their support in the IMF) might wish to press on us and what our reactions should be'.[21]

II

Even before the Suez adventure and its impact on the pound, the British government was considering approaching the IMF for funds to facilitate the transition to convertibility.[22] But by August 1956 the situation was leading to urgent discussion

[18] 'IMF: Statement by Managing Director on Procedures for Reviews of External policies', The National Archives, Kew (hereafter TNA), T354/226; IMF Executive Board Minutes (hereafter EBM), 31 Oct 1973.

[19] Rawlinson to Littler, TNA, T354/226, 12 Sept. 1973. See also TNA, T354/226 Mrs. Hedley-Miller to Mitchell, 'Visit of the IMF Representatives 22 and 23 November 1973', 27 Nov. 1973.

[20] Note to D. Ricketts 8 May 1959, TNA, T236/5740.

[21] C.W. Fogarty to D Mitchell, 21 Dec 1973, TNA, T233/2950.

[22] 'IMF Drawings Against Decreases in Sterling Balances', TNA, T236/5737, 4 May 1956.

of how to deal with the loss of confidence, and as the crisis intensified the need to borrow became overwhelming, and in December 1956 a loan of US$561 million and further standby of $739 million was negotiated. This arrangement was conditional on Britain agreeing to withdraw its forces from Egypt, a condition on which the United States insisted.[23] Interestingly, the French had borrowed from the IMF in October, which made them less vulnerable to the financial pressure which followed over the next couple of months.[24]

The British presented the problem as a short-term loss of confidence in the pound rather than a fundamental difficulty.[25] This interpretation was accepted by the IMF, and support endorsed in the following terms: 'The UK's basic position was sound; a willingness to adopt domestic restraints to deal with economic pressures had been amply demonstrated; and it was only in its role as an international banker that it was in difficulties. The fact that more than half the world's trade is conducted in sterling must be the key to the door of the vault containing the Fund's reserves'.[26] While there was no economic-policy conditionality attached to the December 1956 arrangement (as opposed to a requirement of withdrawal from Suez), it had been preceded by an economic policy statement by the chancellor of the exchequer, Harold Macmillan, announcing further restrictive domestic policies.[27] While arousing much less publicity than later occasions, this statement raised the question of how far Britain in asking for this money had had to make promises to the IMF about the conduct of national policy. Douglas Jay for the Labour Party asked what policy undertakings had been given to the IMF in return for the loan, and was told by Macmillan that the loan was not conditional, although the fund had noted his earlier statement in approving the loan.[28] In February 1957 the Conservative backbencher John Biggs-Davison again suggested that policy was being shaped by IMF conditions.[29] The official view was that the loan had been given *in support* of British policies.[30] In the event, this issue seems to have found little resonance beyond the Tory backbenches, and officials took the view that the less ministers said the more likely was it that the issue would die away.[31]

The IMF had kept a close eye on British developments after the 1956 deal, and while generally supportive of British policy, doubts were expressed about the British authorities' target of a £300 million surplus on current account as well as the government's reasons for not reducing trade discrimination more rapidly.[32] When it came to the United Kingdom's request for an extension of the 1956 deal, support

[23] Kunz, 'Importance', 225–31; Kunz, *Economic Diplomacy*, chs. 5, 6, 7.
[24] Kunz, *Economic Diplomacy*, 102, 113–14.
[25] Foreign Office to Washington 'IMF Stand-by', TNA, T236/5737, 8 Nov. 1956.
[26] IMF, EBM 56/59 10 Dec. 1956, 5.
[27] Statement by Harold Macmillan, 561 *H. C. Deb.*, 5s, cols. 1052–8, 4 Dec. 1956.
[28] 561 *H. C. Deb.*, 5s, col. 327, 18 Dec. 1956.
[29] 562 *H. C. Deb.*, 5s, col. 56, 16 Feb. 1957; ibid., 31 Jan. 1957.
[30] Washington to Foreign Office, TNA, T236/5738, 14 Dec 1956
[31] 'Draft letter to Biggs-Davison', TNA, T236/5379 17 Feb. 1957; 'Conditions for Fund Drawings', ibid., 18 Feb. 1957.
[32] Comments by L. Rasminsky, IMF, EBM 57/10, 27 Feb. 1957, 13–15.

was again forthcoming, although Executive Board members were keen to stress that such renewal was not automatic, and that it should be given on the understanding that Britain was continuing the policies in place at the time of the initial lending.[33]

In 1958 the IMF Executive Board again commended the British policy of restricting demand in order to reduce inflation and improve the payments and reserve positions, and expressed the hope that there would be no early relaxation.[34] By December the board felt able to talk of a 'transformation' in Britain's economic position, and welcomed the trade and exchange liberalisation that had followed. Once again, renewal of the standby was seen as necessary because of the international role of the pound.[35]

The 1950s saw considerable argument in British government circles about the whole approach to economic management, especially on the control of inflation. Part of this argument was about the relative powers of the treasury and the Bank of England to determine monetary policy, and disagreements on this led to the creation of the Radcliffe Committee on the Working of the Monetary System in 1959.[36] A paper submitted to this committee argued that the idea of conditionality on loans to Britain would be 'repugnant to the dignity of a country of the UK's status', and went on to point out that the chancellor had made his policy statement before the 1956 loan was announced. But it continued, 'Nevertheless the Fund is presumably entitled to say that it would not have consented to our drawing if it had not approved of our policies.'[37] The issue was complicated by the fact that the Bank of England was happier than the treasury to see borrowing from the IMF accompanied by a 'letter of intent' (which was not required in 1956). As a treasury official noted, 'I think that I should say flatly that I consider that the Bank are here trying to make sure that the IMF influence will be bought to bear, with a powerful sanction, at future critical junctures, and in particular at a time when HMG is more expansion-minded than the Bank and the IMF.'[38] In other words, the treasury was keen to resist the Bank using the IMF as a lever in domestic policy disagreements.

On the broad issue of the IMF and national autonomy in policymaking, the Radcliffe Report carefully stated the British view in the following terms:

> While the right to draw up to the first 25 per cent of a country's quota is almost automatic, countries have to justify by increasingly stricter criteria any drawings beyond this amount. The use of the Fund's resources does not allow a country the same freedom of action, therefore, as the use of its own reserves. In our view this should not deter the UK from relying upon the Fund and assisting it to play a larger part in the international economy . . . The community of interests that binds together the members of the Fund requires that members who wish to draw on the Fund should be willing to justify to their fellow-members the economic and monetary policies which

[33] IMF, EBM 57/59, 16 Dec. 1957, 2–14.
[34] IMF, EBM 58/11, 7 March 1958
[35] IMF, EBM 58/59, 19 Dec. 1958, 3–16.
[36] P. Burnham, 'The Politicisation of Monetary Policy-Making in Post-War Britain', *British Politics*, 2 (2007), 395–419.
[37] Note to D. Ricketts, TNA, T236/5740, 8 May 1959.
[38] Letter to A.W. France, TNA, T236/5740, ? June 1959.

they are pursuing and that their fellow-members should refrain from imposing unduly rigorous conditions on drawings.[39]

The careful balance suggested in the final sentence was sustainable for the time being, but was to become less so as the 1960s wore on.

1961 was the first year of consultations under Article VIII, and also saw a new request by Britain for a standby arrangement as the expansionary phase of policy accompanying the 1959 general election started to hit the payments position. In support of the British case at the IMF it was argued that 'members should use the Fund as a matter of ordinary business, drawing readily when in need and repurchasing equally readily when the need has passed'.[40]

The IMF willingly agreed what was the largest loan yet given by the Fund ($1,500 million of drawings, $500 million of standby). Some scepticism was expressed as regards the 'short-termism' of British policy, but the dominant feeling was once again that the international role of the pound had to be defended and that domestic policy was facing up to the need to defend it – one member of the Board commending the presence in Piccadilly Circus of a neon sign proclaiming 'Either exports go up, or Britain goes down'.[41] It was, however, pointed out that a key issue for the British payments position was that overseas government expenditure had doubled in ten years; that on aid had shown a similar increase in four years.

The impact on national policy of bargaining with the IMF was raised both by right-wing Conservatives and by the Labour opposition in the Commons. Replying to the former, Selwyn Lloyd, the chancellor of the exchequer, stated that no conditions beyond the terms of repayment had been imposed, although he noted that the facilities had been granted after his 25 July statement.[42] In his question Harold Wilson suggested that 'the Chancellor was able to get this very large loan only in return for promising reactionary policies of a kind which would please certain international bankers'. Unsurprisingly, Lloyd denied this, asserting that 'There was no bargaining about this at all. I made a statement about the policy of the Government, and after the statement was made, the loan was granted.'[43]

Beginning in 1961 the Conservative government began what some historians have called the 'great reappraisal' of British policy.[44] Recent interpretations have stressed the highly conjunctural underpinnings for this 'reappraisal', and also doubts about

39 Radcliffe Committee on the Working of the Monetary System, *Report*, Cmd 827, 1959, 247.

40 IMF, EBM, 4 Aug. 1961.

41 Ibid., 23.

42 648 *H. C. Deb.*, 5s, cols. 787–8, 7 Nov. 1961.

43 649 *H. C. Deb.*, 5s, cols 173–4, 14 Nov. 1961. For discussion of this episode see A. Booth, 'Inflation, Expectations and the Political Economy of Conservative Britain, 1951–1964', *Historical Journal*, 43 (2000), 844.

44 Samuel Brittan seems to have invented this term; see S. Brittan, *The Treasury under the Tories* (Harmondsworth: Penguin, 1964), ch. 7. For recent discussions see H. Pemberton, *Policy Learning and British Governance in the 1960s* (Basingstoke: Palgrave, 2004), and G. O'Hara, *From Dreams to Disillusionment: Economic and Social Planning in the 1960s* (Basingstoke: Palgrave, 2007).

its long-term significance.[45] But in the current context what is important is the overwhelmingly domestic origins of this 'reappraisal', with no evidence that the IMF played a significant role. Brittan's account barely mentions the IMF, and this estimation of the Fund's lack of importance in this episode is borne out by later archival research.[46]

1962 saw a second successive year marked by a standby request. As this request was not forced on the government by an immediate crisis, there was time for a less anxious discussion of the pros and cons. The specific issue was how far the Fund, in return for renewal, would exert pressure on Britain with regard to public spending, which in the early 1960s was growing fast as part of the Conservatives' 'modernisation' policies.[47] As early as March 1962 Per Jacobsson, the Managing Director of the IMF, had written to the chancellor thanking him for his statement on public spending, and stressing how much he believed that 'it is very important to make a long-term programme of restraint in this field and stick to it'.[48] Officials regarded public spending as the key issue in any likely negotiations with the IMF on funding, and were acutely aware of the sensitivities involved.[49] In the event, the application was made, with the treasury taking the view that while the IMF might be expected 'to ask fairly searching questions about the level of public expenditure', 'It is unlikely however that they would push these enquiries to such a point as to make us regret having asked for a standby.' Given that confidence in the pound might be affected by the negotiations over Britain's application to join the European Economic Community (EEC), the balance of advantage seemed to lie with requesting a renewal from the IMF.[50] In the event, the public spending position did not prove a bone of contention.

A further renewal was requested in 1963. The domestic case this time was made in terms of an expansionary policy which the government was trying to prevent from turning inflationary by seeking an agreement on incomes policy, whilst addressing long-term growth by the creation of the National Economic Development Council (NEDC). The broad thrust of this stance was welcomed by the IMF Executive Board, although doubts were expressed about the effectiveness of an incomes policy.[51] The claim was made that the request reflected not a weakness in the current-account position but was made with regard to the international role of the pound and its vulnerability.[52] Britain's representative at the IMF argued that the aim of the renewal was to provide

[45] J. Tomlinson, 'Inventing "decline": The Falling Behind of the British Economy in the Postwar Period', *Economic History Review*, 49 (1996), 731–57; A. Ringe, N. Rollings and R. Middleton, *Economic Policy under the Conservative, 1951–1964* (London: HMSO, 2004), 39–42.

[46] S. Brittan, *Steering the Economy: The Role of the Treasury* (Harmondsworth: Penguin, 1971), 233; Ringe et al., *Economic Policy*; N. Tiratsoo and J. Tomlinson, *The Conservatives and Industrial Efficiency, 1951–64: Thirteen Wasted Years*? (London: Routledge, 1998), ch. 2.

[47] R. Middleton, *Government versus the Market* (Cheltenham: Elgar, 1996), 497–509.

[48] Per Jacobsson to Selwyn Lloyd, TNA, T236/6723, 9 March 1962.

[49] D. Mitchell, 'Renewal of UK Stand-by', TNA, T236/6723 27, March 1962.

[50] 'IMF Standby', TNA, T236/6723, n.d but ?April 1962.

[51] IMF, EBM, 29 July 1963 (afternoon meeting), 7.

[52] IMF, EBM, 29 July 1963 (morning meeting), 3–4.

> an overt sign both of the readiness of the United Kingdom to draw upon the Fund and of the Fund to give immediate assistance. This is in itself a deterrent to speculators and the existence of a substantial standby makes it rather less than more likely that the UK would need to draw upon the resources of the Fund.[53]

The 1963 Letter of Intent pledged the British government to keep the Fund informed of developments, especially on the exchange, trade, credit and fiscal situations and to consult and, if necessary, reach 'new understandings' if there was a major policy shift.[54] This had become the standard form for these letters, again reflecting previous experience on negotiations with the IMF, and in 1963 seems not to have aroused any comment.

The next request for a standby, in 1964, was complicated by the prospect of a general election. The IMF response to the draft Letter of Intent in May 1964 was that it did not put enough emphasis on holding down the inflationary pressures, and criticised the implication that 2–3 per cent inflation was 'all right'.[55] The Treasury feared that this concern with inflation would translate into criticism of the British budget deficit, so the application for a standby focused attention on why the deficit in current circumstances was not inflationary, both because most of the budget deficit would be financed outside the banking sector and because, it was argued, inflation was driven by the conditions of real demand and not monetary expansion.[56]

The normal consultations that summer focused on the impact on inflation and the payments position of continuing rises in demand, although without emphasis on the monetary position.[57] However, discussion at the Executive Board once the standby request had been made did focus some attention on monetary issues, although this was but one among a number of topics discussed.[58] The standby was granted with no difficulties.

III

The election of a Labour government in 1964 inaugurated a more turbulent period in Britain's international economic relations, including with the IMF, and led, among other stratagems, to a temporary tactic of keeping of two sets of data on key economic statistics with the intention of misleading the Fund.

The immediate aftermath of Labour's election victory in October 1964 was marked by a foreign-exchange crisis, quickly followed by the imposition of import charges. Although these charges caused significant international repercussions the IMF was not directly concerned, as the charges were non-discriminatory and had no direct relation to the IMF's concern with financial issues.[59] One member of the Executive Board (Mr Larre) noted how the British account of their current position 'was at

53 'Report of IMF Executive's discussion of 31 July', TNA, T277/1233, 8 Aug. 1963.
54 IMF, EBM, 29 July 2007 (morning meeting), 6.
55 'Mins of meeting 7 May 1964 re draft Statement of Intent', TNA, T311/276.
56 'IMF Standby: notes for Sir Eric Roll', TNA, T311/277, 7 July 1964; IMF, EBM, 27 July 1964, 6.
57 'IMF: UK Consultations 1964 Final Statement by Friedman 12 May 1964', TNA, T277/1440.
58 IMF, EBM, 27 July 1964, 11, 19, 25.
59 IMF, EBM, 28 Oct 1964, 23–4.

considerable variance with the rather rosy description made to the Board at the time of the 1964 Article VIII consultations with the United Kingdom'. As he pointed out, this seemed to amount to a change of circumstances, which would be expected to lead to further discussions with the IMF in line with the Letter of Intent.[60]

IMF concerns regarding the credibility of UK policy focused primarily on the balance of payments. The commitment to achieve balance in international payments by the end of 1966 was a central plank of the government programme. This balance-of-payments objective was also the centrepiece of the May 1965 Letter of Intent to accompany borrowing from the Fund.[61] The UK government fought off quantitative targets on monetary policy, the Letter of Intent referring to 'tight control over bank lending' and 'estimates' for increases in advances to the private sector, but there was no mention of ceilings.[62]

At two IMF Executive Board meetings in May 1965 some executive directors expressed concern that the UK Letter of Intent was too loosely worded, and others expressed scepticism at the United Kingdom's ability to meet its balance-of-payments objective of balance in 1966.[63] In July 1965, after an upwards revision of the deficit forecast, Schweitzer wrote to the chancellor urging further UK government action to achieve the balance-of-payments objectives; 'it is also very clear that the important objective of convincing foreign opinion of the adequacy of the program has not yet been achieved'.[64]

IMF scepticism that the 1966 balance-of-payments objective could be met proved well founded, the basis on which they were making the judgement less so.[65] In preparing for another 'informal visit' in December 1965, UK officials noted that whilst they had 'been *apparently* frank with the IMF', in fact the 1966 balance of payments forecasts given to the Fund in April 1965 'were not on all fours with our then current working forecasts. For the IMF we wrote in a considerably bigger rise in exports than we in fact thought likely.' This raised the delicate issue of 'the extent to which we should expose our latest forecasts showing as they do a continuing deficit in the balance of payments in 1966'.[66] In contemplating the solution, one member of the Treasury team reflects that 'There are obvious difficulties about giving figures which show a failure to reach the Government's publicly stated objective for the balance of payments for the year without being in a position to say what action will be taken to dispose of the deficit. On the other hand, we have learnt a very painful lesson since last April about the practical difficulties of attempting in effect to have

[60] Ibid., 24.

[61] Telegram Foreign Office to Washington, 'The UK drawing from the IMF', TNA, PREM 13/3151, 20 April 1965.

[62] IMF, Archive Executive Board Series (hereafter EBS), /65/74, 2–3.

[63] IMF, EBM/65/25, 23–4, EBM/65/26; Telegram, Sir P. Dean from Washington to Foreign Office, 'IMF: UK Drawing', TNA, PREM 13/3151, 29 April 1965.

[64] Letter from Schweitzer to the UK Chancellor, TNA, T230/800, 14 July 1965.

[65] Mr Hubback to Mr Walker on 'IMF Informal Consultations', ibid., 8 July 1965. See also Telegram Sir P. Dean in Washington to the Foreign Office, TNA, T230/800, 6 Jan. 1966.

[66] P. Brown to Workman, 'The IMF Visit in December', TNA, T230/800, 25 Nov. 1965 (emphasis added).

two sets of books'.[67] UK officials elected to 'come clean (with figures) about the balance of payments' by taking the IMF Mission 'orally through the prospects for 1966 and difficulties of discerning them now in a more or less numberless fashion, but not concealing the possibility of some residual deficit next year'.[68]

Whilst the May 1965 Letter of Intent hinted that external balance would be achieved in 1966 without the import surcharge, the December IMF mission noted that it was now clear that the import surcharge would have to remain, and even then balance would not be achieved. Whittome, the director of the IMF European Department, argued that demand was too high and unemployment too low. The Fund, however, 'recognised that it was entirely up to HMG how the commitment was honoured'.[69]

The strategy of massaging the figures presented to the IMF created as many problems as it resolved, and it was abandoned in November 1965.[70] During 1966 UK government officials sought rather unconvincingly to recast their earlier undertakings, conceding that whilst the 'original target as rigorously defined' would not be 'precisely achieved', it was 'less important to get balance in any particular short period than to achieve the trend of improvement we need to bring us into surplus'.[71] This line was agreed upon by UK officials, so as 'to avoid deceiving the Fund'.[72]

The May 1966 consultations focused on 'how the balance of payments will be restored to equilibrium in the second half of 1966 and how, thereafter, sufficient surpluses will be accumulated'.[73] The IMF mission advocated 'bringing public expenditure under firmer control'.[74] UK policy elites were wary of precise targets for this expenditure because 'the written forecast given last year has proved an embarrassment, and our view is that we might avoid some future embarrassment if we do not give the Fund a formal written memorandum embodying quantified forecasts now'.[75] Balance-of-payments forecasts handed to the IMF team during the consultations were, it was underlined, 'not to be treated as a formal UK forecast but as help to the Fund staff in preparing their report on their own responsibility'.[76]

IMF disquiet at the inadequacy of measures to restrict internal demand remained a significant element in UK–IMF interactions until the balance-of-payments situation improved at the very end of the decade. UK officials countered this with attempts to insert flexibility into undertakings, interpretations and forecasts, but this became more difficult as the nature of undertakings accompanying borrowing increased in scale, specificity and scope in the late 1960s.

67 Ibid.
68 Workman memo to Hubback 'IMF Visit: Balance of payments', TNA, T230/800, 26 Nov. 1965
69 'Note for the Record on IMF consultations by D. Hubback', TNA, T230/800, 7 Dec. 1965.
70 P. Brown to Workman 'The IMF Visit in December', TNA, T230/800, 25 Nov. 1965.
71 Mr. Workman 'IMF Consultations: Balance of Payments', TNA, T230/801, 4 May 1966.
72 Ibid.
73 'United Kingdom – 1966 Article VIII Consultations: Preliminary List of Questions', TNA, T230/720.
74 'IMF: United Kingdom Consultations 1966', TNA, T312/1632, 27 April 1966.
75 Mr. Workman 'IMF Consultations: Balance of Payments', TNA, T230/801, 4 May 1966.
76 Quotes from 'Balance of payments' line in Article 8 consultations, TNA, T230/720.

This tightening of conditionality was a conspicuous feature of the United Kingdom's hotly disputed November 1967 standby arrangement. Early drafts of the UK government's Letter of Intent to the IMF proposed demand-restraining fiscal policy targets as quantified 'trigger clauses'.[77] These were staunchly opposed by the UK chancellor. On monetary policy the chancellor stuck to his 'no quantification of any sort'. Indeed, William Armstrong of the UK treasury even threatened that 'if the Fund insisted on ceilings, the UK might have to do without a standby arrangement'.[78] Tense argument and counter-argument continued at the highest level between the treasury and the IMF. The Fund sought unsuccessfully to secure specific quantitative commitments to reduced government borrowing for 1968, to the diversion of £300 million of resources into tackling the balance of payments, to tax increases and to £4–5 million in spending cuts.[79]

Schweitzer reminded the chancellor that such quantitative targets were standard IMF procedure in the high credit tranches, adding, 'I am concerned that unless this central point is met we would all be courting a new crisis before too long for sterling and the world monetary system as a whole.'[80] The next day, the chancellor told Schweitzer that he could not give the IMF 'information which appears to go beyond what we are able to give to the House. You will understand how extremely damaging an accusation of secret undertakings in relation to an IMF standby could be'.[81]

The Letter of Intent of November 1967 said that 'measures should be taken as and when required' to secure the proposed 'improvement of at least £500 million a year' in the balance of payments. More specifically, it noted that the deflationary government measures announced on 18 November would lead to the 'reduction of home demand by £750 million to £800 million below what would otherwise have been the case'.[82] This forecast was not a 'hard' target. The Letter contains few specific quantitative targets for fiscal policy. The United Kingdom also avoided a phasing of the drawing, reducing the degree to which the UK government was beholden to the IMF in the months following, although the Letter of Intent did involve commitments to reviews in February, July and November 1968.

The borrowing requirement for the financial year beginning April 1968 would be 'kept under firm control', meaning 'not more than £1 billion'. There was an expectation, although not a commitment, that the growth in the money supply would be less for 1968 than it had been for 1967 as a result of measures limiting bank credit which had already been taken.[83]

77 Earlier drafts of Letter of Intent – apparently by WA (William Armstrong), TNA, T326/730, no date.

78 Frank Southard Memo for files 'Proposed UK Stand-By Arrangement: Conversation with Mr Goode,' IMF, Country Files: United Kingdom, File 1760, box 32, 22 Nov. 1967.

79 Frank Southard Memo for files 'Proposed UK Stand-By: Conversations with Mr Goode, November 21 and 22 1967', ibid., 22 Nov. 1967.

80 'Personal message from Schweitzer to the Chancellor', TNA, PREM 13/3151, 22 Nov. 1967.

81 'Personal message from Chancellor to Schweitzer', ibid., 23 Nov. 1967.

82 'United Kingdom – Stand-By Arrangement', EBS/67/277, 29 Nov. 1967, 1.

83 Ibid., 2.

At the November Executive Board some IMF Executive Board members from developing countries called for more precise targets, and questioned whether the proposed measures went far enough. The UK Executive Board director highlighted the 'seal of approval' significance of the standby arrangement at the meeting, noting that 'while the actual facility to draw if necessary is of great importance, it is no more so than the indication that it gives to the world at large that UK policies have the approval and confidence of the Fund'.[84]

Once again questions were asked about the strings attached to the IMF loan. The government line was that policy conditions had not been imposed.[85] Rather, 'in so far as the government's freedom to act is restricted, these restrictions are imposed by the facts of the situation and not by the IMF'.[86] Wilson put the commitments in comparative context: 'we are living in an age when every country comes under scrutiny. Maudling had to send a Letter of Intent in 1964, and so no doubt did Selwyn Lloyd three years earlier.'[87]

Despite public spending cuts in January 1968, the February IMF mission remained sceptical about British policy, notably in relation to 'firm control' of the borrowing requirement.[88] Of this suspicion, treasury officials noted that Fund staff 'believe that . . . our policies have often been shown by events to be insufficient. This strongly-held belief is doctrinal with a certain amount of emotion attached . . . the present scepticism will continue until our own performance proves us right or wrong.'[89] The IMF recommended final expenditure reductions in the order of £500 million in 1968/69 'to put the balance of payments on an unquestionably sound footing and to convince opinion inside and outside the country that this has been done'.[90] By late July 1968, UK officials were expressing disquiet at the strictures of the money supply undertakings given to the IMF, and their adverse unemployment effects (the latter having increased unexpectedly).[91]

Meanwhile top Fund officials, disappointed at the UK government's response to the February 1968 review, considered invoking paragraph 16 of the Letter of Intent. A decision was taken against 'setting in motion procedures for a new formal consultation between the UK and the Fund', because '(a) the Government's political position would be further weakened; and (b) confidence in sterling would be adversely affected'.[92] By the end of 1968 the IMF acknowledged that the government had

84 EBM/67/97, 18–21.
85 'PM's personal minute to the Chancellor on the adjournment debate on the IMF loan', TNA, PREM 13/3151, 4 Dec. 1967.
86 Brief for Ministers by P.R. Baldwin, 'What "strings" or conditions have been attached to the credits from foreign Central Banks and the IMF standby?', ibid.,1 Dec. 1967.
87 'PM's personal minute to the Chancellor on the adjournment debate on the IMF loan', ibid., 4 Dec. 1967.
88 EBS/68/86, 26 March 1968.
89 Hubback to Goldman, 'UK Forecasts and the Fund/OECD February Consultations', TNA, T312/2119, 25 Jan. 1968.
90 Statement by Richard Goode 'IMF Consultations: Final Session', TNA, T312/2120, 27 Feb. 1968.
91 Andrew Graham to Mr Halls on 'Commitments to the IMF',TNA, PREM 13/3151, 26 July 1968.
92 Memorandum from Richard Goode to the Managing Director, 'United Kingdom – Consultations under the standby arrangement', IMF, CF, UK Country files, 1760, Box # 32, File # 5, 10 July 1968.

'acted vigorously in the fiscal area' to restrain demand; 'public expenditure seems to have been well controlled' and 'Heavy tax increases were included in the March budget.'[93] The school report for 1968 still bemoaned 'must try harder', calling for 'continued restraint on demand and on liquidity' deemed 'essential to achieve the further improvement in the balance of payments which is needed'.[94]

In June 1969 the IMF agreed a further standby arrangement, but with a further heightening of the degree of conditionality compared with the November 1967 drawing. The Letter of Intent contained two items expressed in quantitative terms: first, 'an objective of a £300 million balance of payments surplus for current financial year'; second, 'domestic credit expansion is intended to be limited to not more than £400 million in 1969/1970'.[95] A memorandum of understanding was agreed between the IMF mission and UK representatives including quarterly domestic credit expansion targets, which were communicated to the Executive Board but, at the Chancellor's request, not published.[96] Meanwhile, throughout the standby arrangement negotiation process, considerable press coverage raised the 'domestic credibility' issue of the degree to which the Fund would constrain the UK government.[97] There were also questions to the chancellor on this topic in the House of Commons.[98]

The relationship between the 1960s Labour government and the IMF was tense and difficult for much of the time, as the above discussion has emphasised. But if we ask the key question of how far British domestic policy in these years was seriously shifted by the need to sustain credibility with the IMF, the overall conclusion would be that this did not happen. Many of the differences outlined above came down to either the mechanisms or presentation of policy, not its underlying trajectory. Above all, the recognition that devaluation would have to be accompanied by sharply deflationary policies was not the consequence of IMF pressure, but had been recognised by senior ministers and officials as a reason for trying to *avoid* devaluation in the 1964–7 period.[99]

IV

The UK balance-of-payments surplus from late 1969 onwards, coupled with the desire to be freed from intensive IMF scrutiny, led to a happy interlude. During this time Britain 'repurchased all its previous purchases from the Fund. The last repurchase was completed on 28 April 1972. On 23 June 1972, the Fund's holdings of sterling

93 'United Kingdom – Review under standby arrangement', EBS/68/342, 30 Dec. 1968, 20.

94 Ibid., 21.

95 'IMF UK Standby. Statement by the Chancellor of the Exchequer in the House of Commons after questions on 23 June 1969', TNA, PREM 13/3151.

96 'Memorandum of Understanding', TNA, PREM 13–3151, 22 May 1969; 'Memorandum of Understanding', IMF, Country Files: United Kingdom, # 1760, Box 32, 3 May 1969.

97 Victoria Brittain, 'Toughest-Yet Rules on New IMF Stand-by', *The Times*, 11 May 1969; Samuel Brittan, 'IMF to Pose Stiff Conditions for UK Standby Credit', *Financial Times*, 12 May 1969.

98 783 *H.C. Deb.* 5s, cols. 1403–6, 14 May 1969; 'International Monetary Fund (Stand-By Credit)', TNA, T326/979.

99 J. Tomlinson, *The Labour Governments 1964–1970, Vol. 3 Economic Policy* (Manchester: Manchester University Press, 2004) ch. 3, especially 56–7.

stood at 75 per cent of quota.'[100] But then the situation changed rapidly, and the pound was floated. This hinted at credibility and confidence problems for the UK government and its relation to international capital markets. However, these were not deemed to be of a lasting or serious nature at this point, and the IMF Mission report recorded that 'in announcing the decision to float, the Chancellor noted that "there was nothing in the objective facts of our balance of payments position or the level of our reserves to justify these [short-term capital] movements"'.[101]

The floating of sterling added to the sense of an international monetary system in flux. The IMF in this period was seeking to find and define a new role for itself in a radically changed international context, heralded in 1971 by the floating dollar. Fractious discussion of reform of the organisation continued throughout the early 1970s and was not resolved until the new articles of agreement in 1978. The sense of international uncertainty and instability was compounded in 1973 by the Organization of the Petroleum Exporting Countries (OPEC) crisis and the attendant balance-of-payments deficits for many industrial countries.[102] IMF Managing Director Johan Witteveen developed the oil facility, which saw the IMF operate more like a bank, lending at something approaching market rates and with virtually no conditionality.[103] The rationale behind such largely unconditional assistance was to help countries facing balance-of-payments problems arising specifically from the oil crisis. Overall, and to the extent that the distinction could be drawn, the IMF took a more permissive view of balance-of-payments deficits arising from the oil crisis compared with 'normal' payments imbalances.

In Britain the planning process for another drawing from the IMF began in late 1973 under the Conservative government and continued for two years, finally coming to fruition (under a different government) in December 1975. The broad strategy of the Labour government elected in February 1974, in the face of the OPEC crisis imbalances in 1974–5, was to attempt to 'tunnel through' to economic recovery using borrowing (not just from the IMF, but from OPEC governments, and where possible Eurocurrency markets). This came in the context of the 'changed emphasis in the international political economy that encouraged borrowing over adjustment as well as the inflow of OPEC current account surpluses'.[104] The April 1975 budget showed that the government had become convinced of the need to alter policy and cut spending commitments to reduce the scale of necessary borrowing. At the same time, the task of preparing a possible Letter of Intent was once again occupying UK officials. Continued emphasis was placed on less rigidity, avoidance of quantitative targets and summaries of existing government as undertakings. This planned drawing, from the first credit tranche and the oil facility, would involve much lower conditionality than the higher credit tranche borrowings of the late 1960s.[105]

[100] 'United Kingdom – Staff Report for the 1972 Article VIII consultation', IMF, SM/72/155, 27.
[101] Ibid., 25.
[102] James, *International Monetary Co-operation*, ch. 10, 251–5.
[103] De Vries, *International Monetary Fund 1972–78*, 322; Harmon, *British Labour Government*, 65–9.
[104] Harmon, *British Labour Government*, 99.
[105] J. M. Bridgeman to Lavelle, Littler, 'IMF Letter of Intent',TNA, T233/2950, 12 May 1975.

In August 1975 the chancellor explained to Witteveen that 'he had inherited a seriously unbalanced economy. He had decided not to allow the oil crisis to provoke deflation, but had decided to finance the balance of payments deficit.'[106] However, with the failure of the social contract to contain wage pressures, and rising inflation, 'financing was becoming more difficult, with the commercial market unfavourable'. The result was likely to be a 'financing gap in the coming months of around £600 million, or say $1.3 billion, for which the IMF would be a natural source'. In particular, the chancellor was keen not to miss the boat of the oil facility with its very limited conditionality. As further evidence of the complex role played by the IMF in securing domestic credibility, in UK government negotiations to secure spending and wage moderation officials noted that recourse to the IMF presented 'some domestic political problems', not least because 'in discussion of incomes policy and public expenditure, the Chancellor had made some use of the IMF as a threat'.[107]

The prime minister and senior cabinet colleagues discussed a possible IMF drawing in late October 1975. The chancellor, Denis Healey, warned of a likely serious deterioration in the economy in 1977, the only solution being reflation, which would not be possible 'until it was clear to world opinion that the Government's counter-inflation policy was going to be effective'.[108] This again demonstrates the importance of credibility as the cornerstone of government economic strategy, and the centrality of macroeconomic stability to securing it. At this time the importance of credibility was heightened, given the UK government's external borrowing needs. The chancellor considered borrowing from the Euro-currency markets, but noted that 'it was most unlikely that this would be possible before the counter-inflation policy was seen to be successful and the consequences of a rebuff were too serious to make this approach a reasonable risk'. As a result, the IMF was the preferred option. The chancellor pledged to allow 'no obligation to undertake any change to present Government policies', and 'no conditions which would pre-empt future options for direct action on the balance of payments should we wish to take it' in seeking the drawings from the oil facility.[109]

In response to IMF concerns about the public-sector borrowing requirement (PSBR, the gap between government spending and taxation), the treasury noted that 'we are facing more difficulty than oil facility and first credit tranche drawings warrant'. The reason for such difficulties illustrated another dimension of the importance of credibility, in this instance relating to concerns about government control of public expenditure. London identified 'a mood of scepticism' amongst IMF staff 'about our control of PSBR and public expenditure: the Budget forecast of £9 billion PSBR shocked Witteveen; we had to give 10½ billion during talks in August; they do not yet know it but [I] suspect that they are going to be given £12 billion now, and against this history want clear statements'. In this context IMF staff

[106] Rawlinson 'Possible IMF Drawing: Meeting with Witteveen', TNA, T371/23 31, Aug. 1975.
[107] Ibid.
[108] Note of a Meeting at 10 Downing St, TNA, PREM 16/348 28, Oct. 1975.
[109] Ibid.

were 'particularly anxious not to be conned into a political commitment before they know what the illustrative facts will be'.[110]

The four areas of contention at this stage of the preparations for a drawing were, first, the exchange rate, with opinions diverging on both sides about the relative merits of slow or quick depreciation. Second were trade restrictions, to which the IMF was staunchly opposed. The third bone of contention was monetary policy and domestic credit expansion. The fourth was public expenditure and PSBR, given the rise in this noted above.

Some thought was given to pulling out of the planned IMF drawing given the possibility of excessive conditionality, but this view was tempered by the recognition that the United Kingdom only had to demonstrate policy adequate to achieve medium-term balance-of-payments recovery. This constrained the demands IMF staff could reasonably make; 'at least until the end of 1976, with unemployment prospectively rising to 1½ million, the Staff cannot argue the need for additional transfer of resources into the balance of payments through the reduction of public expenditure and increase in unemployment'.[111]

Discussions with the IMF centred on public expenditure and the rising PSBR. Healey stressed the importance of for cash limits on public expenditure, and these, the chancellor told Witteveen, (in terms which were to reappear on the Letter of Application) would 'do much to improve the control of expenditure . . . they would apply to 65 per cent of vote expenditure, including that for local authorities'.[112]

Illustrating the interaction of the two elements of the credibility issue noted above, Witteveen insisted that 'cuts in public expenditure which would produce substantial reductions in the PSBR over the next few years' would 'be necessary to restore confidence in the UK in the international capital markets'.[113] In terms of UK government credibility, damage had been caused by the necessity for dramatic upwards revision of some very public targets during 1975, lending weight to perceptions of spending not being under firm control. Mitchell recorded 'some embarrassment' at 'the discrepancy between the figure of 1.5% increase in public expenditure in 1975/76, and the later revision to 4.4%', not least because these figures were used publicly by the chancellor in the Commons on 21 July 1975, and privately with Witteveen on August 31.[114] However, UK officials felt that they had convinced the IMF 'that this was water over the dam' and thus credibility with the Fund, at least, had been restored.[115]

The upshot of discussion with the IMF was that 'these facilities would be granted without the need for a change in Government policy . . . Nor would there be any restriction on the Government's policies relating to reflation and the sterling exchange

110 Littler, 'IMF Drawing', ibid., 29 Oct. 1975.
111 Ibid.
112 'Note of a working dinner between Chancellor and Witteveen at No 11 Downing Street 3 Nov. 1975', TNA, T371/23.
113 Ibid.
114 Henley to Mitchell 'External use of public expenditure figures', ibid., 4 Nov. 1975.
115 Miss J. E. Court to Mr Anson 'Fund Drawing: public expenditure', ibid., 12 Nov. 1975.

rate'.[116] Quantitative targets for public expenditure cuts and the PSBR was the crux. A figure of £3.5 billion in cuts (which mostly reflected decisions already taken) was discussed and agreed. Witteveen considered inclusion of the figure for public expenditure cuts to be 'a breaking point for his recommending [the UK] application'.[117] Whittome pressed for the Letter of Application to 'say something quantitative, even if only in percentage terms', but Healey resisted, saying that the public expenditure cuts were 'not themselves directly relevant to the first credit tranche, and he did not want to create a precedent'. Instead, 'he would be ready to tell Dr Witteveen and leave him free to tell the Executive Board if that seemed to him desirable'.[118]

In late November 1975, Andrew Graham, a treasury adviser, expressed strident opposition to some of the contents of the mooted IMF Letter of Application, in particular the proposed commitment not to exceed 'an absolute figure' (of £12 billon) for PSBR for 1976/77;

> This *must* be resisted because (a) it would tie the Government's hands almost completely (and wholly unreasonably) on reflation, and (b) a new forecasting round is just starting and this might show a PSBR above £12 bn in 1976/77. If it did, we would have to deflate in the next budget.

He also resisted phased payment, which 'could be conditional in a variety of ways' and 'the purse strings could even be tightened as we go along'; he concluded, exasperated, 'it is crazy to allow this letter of *application* to become one of intent. How low have we sunk?'[119]

In December 1975 the UK government applied for a drawing of special drawing rights (SDRs, the reserve asset created by the IMF) of 1,000 million under the oil facility, and a standby arrangement for a further SDR 700 million (1 SDR = approximately $1.2). The letter of application, which combined the oil facility and first credit tranche applications, said explicitly that it merely summarised existing policy commitments of the government set forth by the chancellor and the prime minister. It had, one official noted, 'been deliberately loosely drafted as an exposition of present policies and the way we see things going, and not as a set of undertakings in any respect'.[120] As per earlier drafts, the Letter of Application identifies the government objectives of 'a reduction in the rate of unemployment' and a 'marked improvement in the balance of payments position', as well as explicit mention of 'full employment' as an objective.[121]

The control of public expenditure, and the government's 'extensive use of cash limits in 1976–77 . . . [on] about three quarters of central government voted expenditure' was set out in the letter. Although precise quantitative figures are absent,

116 'Note of a Meeting in the House of Commons 5 Nov. 1975', TNA, PREM 16/348.
117 'NLW(?) to Prime Minister', TNA, PREM 16/827, 19 Dec. 1975.
118 C.W. France, 'Mr. Witteveen's call on the Chancellor', TNA, T371/23, 20 Nov. 1975.
119 A. Graham to Mr Stowe 'Letter to the IMF', TNA, PREM 16/348, 21 Nov. 1975 (emphasis in original).
120 'NLW (?) to Prime Minister 18 Dec. 1975', TNA, PREM 16/827.
121 Healey to Witteveen 'Letter of Application', ibid., 18 Dec. 1975.

the Letter noted that 'substantial reductions must be made in the public expenditure programmes . . . Total public expenditure at constant prices (excluding debt interest) will now be planned to remain, in 1977–78 and 1978–79, no higher than the level now planned in 1976–77.'[122] Treasury memos hinted that *some* of the agreed figure of £3.5 billion did represent new cuts, referring to

> a risk of embarrassment if the figure of £3.5 billion were to leak through the Executive Board, and subsequently were to be compared with the savings shown in the White Paper by comparison with CMND 5879. In particular, the £500 million saving on social security cannot be publicly revealed.[123]

Overall, however, the Letter avoids tight constraints in relation to both public expenditure and the borrowing requirement. Caveats were inserted to alleviate earlier anxiety about PSBR targets.[124] On the monetary policy front, whilst there was reference to domestic credit expansion, Healey pointed out to Wilson that 'I was able to insist that, for a letter applying only for the first credit tranche, greater detail and firmer undertakings were not required.'[125] The IMF Executive Board meeting which discussed the UK drawing supported it, and praised UK policy.[126]

Concerns about the creditworthiness of the UK government hampered the attempted strategy of 'tunnelling through' the oil crisis difficulties. The principal problems facing credibility were two fold, relating to inflation on the one hand and public spending and the borrowing requirement on the other. The 1975 public statement of the counter-inflation strategy, *The Attack on Inflation* (Cmnd. 6151, July 1975), was the government's attempt to address the first issue. The negotiations with the IMF constituted one forum where the second credibility problem was addressed. This was hampered by damaging revelations of underestimated deficits. By the end of the process the UK policymakers felt that they had convinced the IMF of UK control of public expenditure, and they also expected that the agreement on the drawing would provide the 'seal of approval' on UK policy necessary to convince international capital markets of the stability and sustainability of the UK policy regime. This award of a seal of approval was, as has been noted, to become the key outcome of the story of 1976.

V

Between 1956 and 1976 Britain pursued a policy of fine-tuning of the national economy while simultaneously liberalising its international transactions. Given the aim of sustaining sterling as an international currency while committing large amounts of foreign exchange to overseas investment, military expenditure and development aid, the payments position in this era was always falling below the hopes and ambitions of policymakers, causing crises of confidence and entailing recourse to international

122 Ibid.
123 Telegram Littler to France & Callaghan, 'IMF Drawing', TNA, PREM 16/827, 16 Dec. 1975.
124 Healey to Witteveen 'Letter of Application', TNA, PREM 16/827, 18 Dec. 1975.
125 Healey to Wilson, 'IMF Applications', ibid., 2 Jan. 1976.
126 Telegram UK Director IMF Ryrie 'IMF Drawing', ibid., 31 Dec. 1975.

support. In the immediate aftermath of the war this assistance came from the US loan and Marshall Aid, but in the period thereafter the IMF was the key agency of support. To obtain that support required negotiating credible policy positions with the Fund while simultaneously maintaining domestic political credibility by asserting the sovereignty of the national government over economic policy.

Until 1965 sustaining these 'two credibilities' was not very difficult. The role of sterling gave Britain substantial bargaining power; the IMF, as guardian of the international monetary system, could not permit the collapse of the world's second most important currency. At the same time, the Fund's own overall stance was one of 'low conditionality', and such conditionality as was imposed was negotiated bilaterally, with little uniformity of treatment. In turn this meant that the British government had little difficulty sustaining domestic political credibility; the grumbling of a few backbenchers and opposition MPs was the worst governments had to face. Any idea that British governments in this period were forced into significant policy concessions in return for IMF help would be unsustainable.

After 1965 the position shifted. The IMF tightened up its policies on conditionality and at the same time became less willing to treat Britain as exceptional. The desire to support Britain's defence of sterling remained, but the willingness to allow defence of that role to be used as a reason for 'going easy' on the British diminished. Also, the mid-1960s saw some weakening of Britain's overall balance-of-payments position, although again it is worth emphasising how much the problem was over-ambitious policy goals coupled with the vulnerability flowing from the reserve role of sterling, rather than any major deterioration in international competitiveness.

Another element in the tensions of the 1960s was the advent of a Labour government, always more subject to pressure to demonstrate the 'responsibility' of their financial policies, while simultaneously subject to greater pressure than Conservative governments to pursue domestic policies likely to be at odds with international financial opinion. Linked to this was a degree of ideological divergence between the British government and the IMF over economic policy. A form of 'monetarism' was emerging in the counsels of the IMF, which involved not only a focus on monetary aggregates, but, perhaps even more importantly, a scepticism about governmental discretion in the conduct of economic policy and an enthusiasm for fixed, quantitative targets. Nevertheless, as argued above, these pressures from the IMF cannot plausibly be said to have fundamentally shaped British domestic policy in the late 1960s. Above all, the post-devaluation debate was mainly about how deflation should be achieved, rather than whether it was the right policy.

There are clear continuities in the debates of the late 1960s and those of the mid-1970s. In both periods the uncertainty of the macro-economic environment made predicting outcomes almost impossible, and made the British government extremely wary of tying itself to the numerical targets that the IMF had come to favour. This issue of national discretion in policy *formulation* was significant, but must not be conflated with contention over policy *objectives*.

The problem of 1976, to reiterate, was not that the IMF as forcing a new and uncongenial policy direction on the Labour government. By the time of the IMF visit, policy was clearly giving priority to reducing inflation, which was on a downward path, and public-sector finances were rapidly improving following the fiscal packages of 1975 and 1976, and the imposition of cash limits on public spending. But the government had to restore international confidence, and the support of the IMF was vital for this. Juggling this necessity against the domestic political hostility aroused by dis-inflationary policies was the core issue in 1976. But despite the dramas of that year, what occurred in 1976 does not in essence detract from the conclusion that, while credibility was a vital goal of the authorities from the time of the Suez crisis to the Callaghan period, its achievement did not push British policy on to paths which would otherwise have been untrodden. Cairncross and Burk's conclusion on 1976, that 'Apart from the continued issue of monetary targets, which were rarely hit, economic policy in the last years of the Labour government differed little from what it had been before the arrival of the IMF', could be applied to all previous episodes of borrowing. In these years, the price of IMF credibility was small.[127]

The question which this conclusion about the British case raises is how generally it might apply. France would appear to be a particularly interesting comparator, as it was also a big borrower from the IMF in these years, but was without the burden or benefits of a reserve currency. In the British case, the IMF desire to sustain sterling's international role proved a powerful bargaining chip in the battle to sustain domestic control over policy. In the French case, did the absence of this chip seriously weaken sustaining such control?

[127] Burk and Cairncross, *Goodbye Great Britain*, 228.