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Settlements, 1930-1973
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Central Bank Cooperation at the
Bank for International Settlements, 1930–1973

This book covers the history of the Bank for International Settlements (BIS), the first-born among international economic institutions, from its founding in Basel in 1930 to the end of the Bretton Woods system in 1973. While the focus is on cooperation among the main central banks for the stability and efficiency of the international monetary system, this book also offers an institutional history of the BIS. The first chapters explore the foundation of the BIS, its role in the financial crisis of 1931, the London Economic Conference of 1933, and the following years when central bank cooperation was reduced to mostly technical matters. Considerable attention is devoted to the much-criticised activity of the BIS during World War II. The book then deals with the intensive central bank cooperation for the re-creation of Europe's multilateral payments in the 1950s and for the support of the Bretton Woods system in the 1960s. The last chapter is devoted to the involvement of central banks in the first timid steps towards European monetary unification and to the eurodollar market.

Gianni Toniolo is Professor of Economics at the Università di Roma Tor Vergata (Italy) and Research Professor of Economics at Duke University. A former Professor of Economics and Chair of the Economics Department at the University of Venice, he has held visiting positions at All Souls College and St. Antony's College, Oxford; Hitotsubashi University, Tokyo; the University of California at Berkeley; and the University of Connecticut. He is also a Research Fellow of the Centre for Economic Policy Research in London and a member of the European Academy. Professor Toniolo is the author of several books on European and Italian economic growth from 1800 to the present and on the history of financial markets and institutions with special reference to central banking, including *The European Economy between the Wars* (1997, with C. H. Feinstein and P. Temin) and *An Economic History of Liberal Italy, 1850–1918* (1990). He is the editor of 17 books, including *Patterns of European Industrialization: The Nineteenth Century* (1991, with R. E. Sylla), *Central Banks' Independence in Historical Perspective* (1988), and *Economic Growth in Europe Since 1945* (Cambridge University Press, 1996, with N. Crafts). Professor Toniolo is co-editor (with P. Ciocca and G. Federico) of *Rivista di Storia Economica*.

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GIANNI TONIOLO

*Università di Roma Tor Vergata,
Duke University, and CEPR*

with the assistance of
Piet Clement



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 Frontmatter
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Contents

<i>List of Figures and Tables</i>	<i>page</i> xi
<i>Foreword</i>	xii
<i>Preface</i>	xv
<i>List of Acronyms</i>	xxi
1 International Payments and Central Bank Cooperation	1
1.1 A BIS View of Cooperation	1
1.2 International Monetary Systems, 1870–1973	5
1.3 Reasons and Conditions for International Monetary Cooperation	9
1.4 Central Bank Cooperation under the Classical Gold Standard	13
1.5 Central Bank Cooperation, 1914–1922	16
1.6 The “International Bank”: An Old Cooperative Idea	20
2 Gestation and Birth	24
2.1 The Background	24
2.2 The Young Committee	33
2.3 The Baden-Baden Committee	39
2.4 American Ambiguity	44
2.5 The Legal Basis	48
2.6 High Hopes Are Raised: Comments on the Creation of the BIS	52
2.7 Outlook and Expectations	56
3 Organisation and First Operations	61
3.1 Off the Ground	61
3.2 People and Organisation	63
3.3 The Capital of the Bank	67
3.4 Dealing with Reparations	70
3.5 The Banking Side	72
3.6 The Issue of Long-Term Lending	74
3.7 The Peseta	77

Cambridge University Press

0521845513 - Central Bank Cooperation at the Bank for International
Settlements, 1930-1973

Gianni Toniolo

Frontmatter

[More information](#)

viii

Contents

4	The 1931 Crisis and International Lending	84
4.1	The Background	84
4.2	The BIS as International Lender: The Credit-Anstalt Crisis	88
4.3	Lending to Hungary, Yugoslavia, and Danzig	97
4.4	The BIS and the German Financial Crisis	100
4.5	Assessing the First BIS Experience as Crisis Manager	106
5	The End of Reparations, the Gold Standard, and the 1933 London Conference	115
5.1	The End of the Interwar Gold Standard	115
5.2	Facing the New Reality	119
5.3	The Wiggin Committee	123
5.4	The Beneduce Committee and the Lausanne Conference	127
5.5	Custodian of the Gold Standard	131
5.6	The Preparatory Commission of Experts for the London Conference	136
5.7	The BIS at the London Conference	144
5.8	The Bank's Role as Trustee and the German Transfer Crisis	149
5.9	Emphasis on Cooperation	157
6	An Autarkic and Divided World	159
6.1	Strained International Relations	159
6.2	Central Bank Cooperation in an Autarkic World: An Oxymoron?	162
6.3	The United States and the BIS	167
6.4	The Tripartite Agreement	175
6.5	People and Organisation	183
6.6	The Banking Side	185
6.7	Clearing Agent for the Universal Postal Union	189
6.8	The Monetary and Economic (Research) Department	191
6.9	The Governors' Unofficial Meetings	195
7	Wartime	201
7.1	Neutrality and Cooperation	201
7.2	The Czechoslovak Gold Affair	204
7.3	Neutrality Declaration and Policy	213
7.4	Enemies under the Same Roof: Wartime Daily Life at the BIS	220
7.5	Belligerents' Diplomacy: McKittrick's Reappointment	224
7.6	The BIS and the Axis	226
7.7	The BIS and the Allies	232
7.8	The BIS, Switzerland, and the Other Neutrals	235
7.9	Wartime Business Activity	238
7.10	Wartime Gold Transactions with the Reichsbank	245
7.11	Italian Gold	252
7.12	Assessing the BIS's Wartime Conduct	256

	<i>Contents</i>	ix
8	Bretton Woods	260
8.1	The Road to Bretton Woods	260
8.2	The BIS at Bretton Woods	267
8.3	After Bretton Woods	271
8.4	The Restitution of Looted Gold	276
8.5	What “Saved” the BIS?	279
9	Reconstructing Multilateral Payments	283
9.1	Europe’s Reconstruction and International Settlements	283
9.2	The Postwar Economy in the Analysis of the BIS	286
9.3	Central Banks: <i>Plus ça change ...?</i>	291
9.4	Early Postwar Activity	297
9.5	The 1947 Agreement on Multilateral Monetary Compensation	301
9.6	The OEEC and the 1948 Agreement for Intra-European Payments and Compensations	305
10	Achieving Convertibility	309
10.1	Europe’s “Golden Age” and International Payments	309
10.2	International Monetary Cooperation	312
10.3	The BIS in the 1950s	317
10.4	Economic Analysis	323
10.5	The Birth of the European Payments Union	327
10.6	Central Banks, the BIS and the EPU	333
10.7	The EPU in Operation	335
10.8	Convertibility and the European Monetary Agreement	339
10.9	Eastern European Central Banks and the BIS	346
11	The 1960s: Patching Up the Bretton Woods System	350
11.1	The International Monetary System, 1959–1973	350
11.2	The BIS in the 1960s	357
11.3	The “Basel Club”	363
11.4	1960–1961: The European Rescue of the Dollar	369
11.5	Origin and Operations of the Gold Pool	375
11.6	Mutual Support: The Basel Agreement, Swap Networks, and “Bilateral Concerté”	381
11.7	The Defence of Sterling	388
11.8	The BIS, the G10, and the Debate on Reforming the International Monetary System	399
11.9	1968: The Beginning of the End	410
11.10	The BIS Role in the Second Sterling Group Arrangement	423
11.11	The French Franc and the Deutsche Mark	426
11.12	The End of Bretton Woods	428
12	Monetary Union and Financial Stability	437
12.1	At the Roots of the BIS’s Future	437
12.2	The EEC Governors’ Meetings in the 1960s	439

Cambridge University Press
0521845513 - Central Bank Cooperation at the Bank for International
Settlements, 1930-1973
Gianni Toniolo
Frontmatter
[More information](#)

x	<i>Contents</i>	
12.3	The Werner Plan and European Monetary Integration	444
12.4	The Eurocurrency Market	452
12.5	Central Banks' Concerns about the Eurocurrency Market	455
12.6	Filling the Information Gap	457
12.7	The Eurocurrency Market and Monetary Policy	460
12.8	Prudential Issues	469
	<i>Epilogue</i>	473
	<i>Notes</i>	489
	<i>List of Archives Consulted</i>	613
	<i>Bibliography</i>	617
Annex A:	BIS Statutes 1930	635
Annex B:	BIS Balance Sheet, 1930–2000	647
Annex C:	BIS Board of Directors and Management, 1930–2005	661
Annex D:	Chronology of Events, 1929–2005	667
Annex E:	Dramatis Personae: Biographical Sketches	697
	<i>Index</i>	713

Figures and Tables

FIGURES

3.1	BIS “organigram”, 1933 (reconstruction)	<i>page</i> 64
10.1	BIS “organigram”, 1955 (reconstruction)	322
11.1	BIS Gold Pool operations and London gold price, 1960–73	419
12.1	BIS “organigram”, 1969 (adaptation)	440
B.1	Evolution of BIS balance sheet liabilities and net profits, 1931–58 (millions of U.S. dollars at current prices)	654
B.2	Evolution of BIS balance sheet liabilities and net profits, 1959–80 (millions of U.S. dollars at current prices)	656
B.3	Evolution of BIS balance sheet liabilities and net profits, 1980–2003 (millions of U.S. dollars at current prices)	658

TABLES

4.1	Central bank credits organised through or with the participation of the BIS, 1931	108
5.1	Receipt and distribution of German funds for reparation payments and loans service, 1930–34	156
7.1	BIS gold shipments, June 1938–June 1940	240
7.2	Wartime movements on the Reichsbank gold account at the BIS	246
11.1	U.K. reserves, sterling balances, and international support organised through or with the BIS, 1961–71 (millions of U.S. dollars at current prices)	396

Cambridge University Press
0521845513 - Central Bank Cooperation at the Bank for International
Settlements, 1930-1973
Gianni Toniolo
Frontmatter
[More information](#)

Foreword

In 2005, the Bank for International Settlements, the world's oldest international financial institution, celebrates its seventy-fifth anniversary. The central bankers who gathered around the BIS meeting table in Basel, Switzerland, for the first time in May 1930 shared a vision that endures to this day. They created an institution that provided them with valuable services in international banking and research while serving also as a meeting place where they could discuss monetary policy issues amongst peers and cooperate effectively whenever necessary. The BIS has played this dual role of service provider and meeting forum for central banks ever since its foundation 75 years ago, and it continues to do so while moving forward to meet new challenges.

In 1980, on the occasion of its fiftieth anniversary, the BIS asked Paolo Baffi – a long-serving BIS Board member, former governor of the Bank of Italy, and outstanding economist – to write the history of the Bank. Unfortunately, Baffi died while his work on the BIS was still at an early stage. The idea of having the Bank's history written was revived under the impulse of my predecessor Andrew Crockett. In 1999, the BIS entrusted this task to Gianni Toniolo.

The book covers the years 1930 to 1973: from the foundation of the Bank until the end of the Bretton Woods monetary system. In writing the BIS's history during this period, Professor Toniolo has made extensive use of the Bank's archives. He also greatly benefited from close and productive collaboration with Piet Clement, Head of Library, Archives & Research Support at the BIS and himself an experienced historian.

In this book, Gianni Toniolo has succeeded in disentangling the sometimes complex and technical issues that are at the core of central banking,

placing them in their broad historical context. At the same time he has provided a clear and often compelling narrative that makes this book accessible and worthwhile to layman and specialist alike.

It is a good thing to look back once in a while. By gaining a better understanding of the past – its successes and its setbacks – we are able to make a more balanced judgment of the present and, it is hoped, to look with more confidence to the future. Moreover, for an international organisation such as the BIS, it is a healthy and instructive exercise to have its past performance evaluated by an external expert such as Professor Toniolo, who has really steeped himself in the Bank's history. It goes without saying that the author's views do not necessarily reflect those of the BIS or of its member central banks. Having said that, I believe that Gianni Toniolo's review of more than four decades of central bank cooperation at the BIS offers a sober judgment and provides many thought-provoking insights.

In my view, the book's most important message is that, in the interconnected world of the twentieth and twenty-first centuries, international cooperation (even if does not always yield tangible results) is far preferable to the alternatives of indifference or, worse still, confrontation. The 1930s are a case in point. Indeed, when the need for cooperation in the economic and financial field was more generally recognised – as was the case in the Western world in the 1950s and 1960s – central bank cooperation as fostered by the BIS contributed significantly to a better understanding, and reduced areas of conflict, among different nations and thereby to positive spillover effects on the global economy as a whole. In any case, effective international cooperation is never to be taken for granted.

The central banks and the BIS can look back with some pride at several successes in this cooperation. Achievements such as the European Payments Union are given due recognition in Toniolo's work. It can be argued, however, that it is the frank and open exchange of views, the comparison of experiences, and the formal and informal meeting opportunities under the auspices of the BIS that have immeasurably helped the central banks execute their responsibilities, with due regard to the international environment in which they operate and with due attention to the implications of their actions for others.

As far as the BIS is concerned, it is encouraging to see that – by remaining small, flexible, and free from political interference – the Bank has, throughout its history, succeeded remarkably well in adapting itself to evolving circumstances. Thus, the BIS has transformed itself in recent years from a predominantly European organisation into a global forum for discussion reaching out to the entire community of central banks. Moreover,

Cambridge University Press
0521845513 - Central Bank Cooperation at the Bank for International
Settlements, 1930-1973
Gianni Toniolo
Frontmatter
[More information](#)

xiv

Foreword

in addition to its focus on “traditional” monetary policy issues, the BIS has become ever more deeply involved in supporting the efforts of central banks and financial supervisors to fulfil their joint responsibilities in the area of financial stability.

Since the financial industry has grown rapidly in size, complexity, and sophistication, it is widely recognised that nurturing the right incentives for sound financial behaviour and for managing risks and returns in a global and competitive world requires close cooperation among central banks and between them and other financial authorities. The BIS has an important role to play in the general monitoring of the global financial system, but it is especially in the areas of banking regulation, market functioning, and the payment and settlement infrastructure that central banks and other financial standard setters have relied on the services of the BIS and the committees it hosts. A prominent example of this is the recent formulation of a new capital adequacy framework for banks (“Basel II”).

The ability to adapt when change is required and to always place the needs and requirements of its constituency centre stage is also the main reason why I am convinced that the BIS still has a long and fruitful future before it.

It gives me great pleasure to commend Gianni Toniolo’s history of the BIS to the widest possible audience of interested readers.

Malcolm D. Knight
General Manager of the BIS

Basel
November 2004

Preface

One early December night I woke up in North Carolina feeling uncomfortably cold. I reached for the light switch but the room remained dark. Still half asleep, I crept downstairs to check on the fuses, and I became aware that all around me was white and that it was still snowing heavily. I soon found out that there was nothing wrong with my fuses: no light came from any of the neighbours' windows, and the street lamps were out. In the following hours, battery-powered radios informed us that more than a million people in the area were cut off from power supply. Light, cooking facilities, heating, and running water were all gone. The network had collapsed. Under the weight of the snow, tree branches had broken off, disrupting the intricate web of electrical wires that connect individual houses with the local power lines as well as the latter with the main ones. It took several days of round-the-clock work by electrical engineers – and the cooperation of teams from neighbouring states – for light and heat to be restored to homes, schools, and offices. In the meanwhile, life was reduced to basics, if in a rather pleasant way. Most of the time was spent hunting for food and water, checking on friends, and sharing the heat in the houses of those lucky enough to possess such archaic items as coal- and wood-burning stoves.

At first, I was surprised at how easily, in twenty-first-century North America, a banal snowstorm could bring a large, sophisticated urban area back to the nineteenth century. But it soon occurred to me that one should be more surprised by the day-to-day functioning of a complex power distribution network than by its occasional failure. Our civilisation is largely based on network technology, which – though now developed to high degrees of sophistication – remains intrinsically vulnerable. Failure at just one of the connecting nodes is bound to incapacitate large segments of the net. An

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Settlements, 1930-1973

Gianni Toniolo

Frontmatter

[More information](#)

act of God or man can only too easily disrupt the flow of energy, information, fuel, merchandise, and people so vital to our daily life, as is routinely observed in large areas of the world.

The payments system is yet another complex network technology, one based upon sophisticated technical tools, market mechanisms, and institutional arrangements. We take it for granted that our cheques clear, that ATMs instantly provide cash anywhere in the world, that imports are paid for in the required currency, and that the desired amount of liquidity is available to us at any time at the lowest cost. But all this is far from being a given, far from being put in place once and for all. In fact, as with the power grid, we should marvel at the ordinarily smooth working of the international payments network rather than be surprised at its occasional malfunction.

In the wake of the 11 September 2001 attacks on the Twin Towers, the main central banks of the world issued a joint statement pledging unlimited supply of liquidity for international settlements. It was an exemplary display of prompt cooperation that was aimed at pre-empting a scramble for liquidity that would impair the payments network. Such swift cooperative action has not always been taken in past emergencies. Although central banks cooperated effectively in reorganising Europe's international settlements in the 1950s and in maintaining dollar-gold convertibility in the 1960s, their prewar record is much less shining. They were unable to prevent or mitigate the financial crisis of 1931 and the subsequent unravelling of the international payments system.

This book is about the successes and failures of central bankers in cooperating to maintain the stability and promote the efficiency of that delicate network that constitutes the system of international payments, of which they are the ultimate custodians. Since 1930, the main locus for multilateral central bank cooperation has been the Bank for International Settlements (BIS), which has provided central bankers with a venue for regular and discreet meetings, with research on issues relevant to international payments, and with a collective financial arm (as the "central banks' bank"). This book is therefore also an institutional history of the BIS from the time of its foundation in 1929-30 to the end of the Bretton Woods system in 1971-73.

The chapters follow a chronological sequence: I know of no better historical narrative than that which takes time seriously. Within each chapter, however, the material is organised to a large extent by subject matter, dealing separately with the most relevant issues in central bank cooperation and with the Bank's internal development and organisation. The first section in each chapter provides a general historical background to the events in the BIS history to be discussed in subsequent sections. The first and the last

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0521845513 - Central Bank Cooperation at the Bank for International
Settlements, 1930-1973

Gianni Toniolo

Frontmatter

[More information](#)*Preface*

xvii

chapters do not follow the same paradigm as the others. Chapter 1 is designed to offer a brief introduction – based more on history than economic theory – to the themes of international payments and central bank cooperation. Chapter 12 deals with two topics not previously touched upon: the early moves towards cooperation among the European Community central banks, and the meteoric rise of the eurocurrency market. The reason for dealing separately with these two topics is found in their relevance for the development of central bank cooperation beyond the period covered in this book.

The analytical narrative stops in 1973; the reader interested in the subsequent history of the BIS will only find a concise chronology of the main events. There is more than one reason why the end of this book should coincide with that of the Bretton Woods system. On the one hand the book, and its underlying research effort, seemed to have already taken on considerable dimensions; on the other hand, 1973 marked a discontinuity not only in the history of international payments but in that of the BIS as well. However, the main reason for pausing in the early 1970s concerns the availability of primary sources, which generally are subject to the 30-year disclosure rule of the main archives visited for this research. In particular, the BIS archives – explicitly protected by the Bank's Statutes – were opened to the public in 1997, but only for records older than 30 years.

This book was largely written in Basel, a pleasant and lively city that I learned to enjoy. For a few years it became almost my second home. The Bank for International Settlements provided me with an exceptionally friendly and stimulating work environment, a most comfortable office, and all the research assistance I could dream of, but at the same time it granted me absolute freedom of research and writing. General Managers Andrew Crockett and Malcolm Knight could not have been more encouraging and supportive while simultaneously respecting and protecting the independence of my research. The views expressed here are thus my own and do not necessarily reflect those of the BIS management and member central banks.

In researching for and writing this book I accumulated a huge debt of gratitude to the large number of people who in various capacities and ways provided support and intellectual input to my work.

Piet Clement went far beyond the duties of a technically competent and intellectually refined research assistant. The chapters dealing with the London Economic Conference, the Second World War, the 1960s, and the EEC governors' meetings would probably not have seen the light of day without his essential contribution (which, however, does not imply any responsibility on his part). Piet's involvement was also invaluable in archival research,

Cambridge University Press

0521845513 - Central Bank Cooperation at the Bank for International Settlements, 1930-1973

Gianni Toniolo

Frontmatter

[More information](#)

xviii

Preface

all over the world, and in bridging my German and Dutch language gap. The friendship we developed over the years is yet another gift coming from this project. Piet's wife, Greet Van Malderen, also deserves my gratitude for sharing with him the burden of his research.

Edward Atkinson provided superb archival assistance, was indispensable in organising my life in Basel, and contributed the *Dramatis Personae* (Annex E). I also enjoyed his proverbial English wit. Relevant and competent research input was provided by Michelangelo Van Meerten on the origin of the BIS and Stefano Battilossi on the eurodollar market. Kazuhiko Yago offered insightful comments and materials on matters pertaining to Japan. Leandro Conte and Marina Sorrentino served ably as research assistants at an early stage of the project.

My special thanks go to the friendly and supportive staff of the BIS Library and Records and Archives teams, and in particular to Maria Friesen, Arwen Hopkins, and Johannes Koch. Unobtrusively behind the scenes, Alan Mortby quietly made sure that I enjoyed all the support I needed. I am also grateful to the BIS Secretarial Service, Language Services, and print shop as well as to current and former staff members from other services for comments and assistance – in particular, Frederick Adelman, Stephan Arthur, Joseph Bisignano, Paul Bridge, Raymond Fin, James Freis, Angela Maramag, and Jozef Van 't dack. Nigel Hulbert patiently and efficiently took care of the first round of editing of the manuscript.

Research at the BIS was extensively supplemented by a considerable number of other archival sources, in particular those of the main central banks and of several governmental institutions. This additional research was made both possible and agreeable by the professional and friendly assistance of Walter Pluym and Christa Asselman (National Bank of Belgium); Rolf Herget and K. Fitzner (Deutsche Bundesbank); Henry Gillett and Sarah Millard (Bank of England); Roland Rölker and Mascha Steinecke (European Central Bank); Mme. Cavillon-Troade, Frédéric Grélaud, and Fabrice Reuze (Bank of France); Olivier Feiertag (Historical Mission of the Bank of France); Gabriella Raitano and Sergio Cardarelli (Bank of Italy); Floris Joustra, Joke Mooij, Corry Van Renselaar, and Rian Beex (Netherlands Bank); Rosemary Lazenby and Joseph Komljenovich (Federal Reserve Bank of New York); Teresa Tortella (Bank of Spain); Mira Barkå (Sveriges Riksbank); Patrick Halbeisen (Swiss National Bank); Frau von Boeselager (Auswärtiges Amt, Berlin – Politisches Archiv); Martin Steinmann, Franz Gschwind, and Tamara Rodel (Basel University Library, Handschriftenabteilung); Brent Svertloff (Harvard University Baker Library); Herr Roeske (Bundesarchiv Berlin); Frau Oldenhage (Bundesarchiv Koblenz);

Cambridge University Press

0521845513 - Central Bank Cooperation at the Bank for International
Settlements, 1930-1973

Gianni Toniolo

Frontmatter

[More information](#)

Preface

xix

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A special thought goes to the memory of Paolo Baffi, who would have written this book much better than I did; for many of us in Italy he remains a hallmark of civil passion and intellectual integrity.

My debt to Francesca Sanna Randaccio – the companion of my life and a superb economist – is *also* intellectual. Its full extent can be entirely appreciated only by the two of us. Paolo quietly understands that I owe him a lot.

The book appears at a time when, in a number of areas, the drive to strengthen multilateral international relations is at risk of losing momentum. I hope it will make a small contribution by showing that, in a tightly networked world, there is scarcely any better alternative to painstakingly seeking multilateral cooperation. The events of the 1930s serve to remind

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Settlements, 1930-1973
Gianni Toniolo
Frontmatter
[More information](#)

xx

Preface

us that go-it-alone, autarkic, beggar-thy-neighbour policies are suboptimal for all and everybody. I also hope the book makes it clear how much patience, perseverance, and strength in weathering setbacks is required of the people – such as those who go on meeting regularly at the BIS in Basel – whose mission it is to build a more cooperative multilateral world.

Acronyms

ANB	Austrian National Bank
BCBS	Basel Committee on Banking Supervision
Benelux	Belgium, the Netherlands, and Luxembourg
BIS	Bank for International Settlements
BIZ	Bank für Internationalen Zahlungsausgleich (BIS)
BRI	Banque des Règlements Internationaux – Banca dei Regolamenti Internazionali (BIS)
C20	Committee of Twenty
CEEC	Committee of European Economic Co-operation
CGFS	Committee on the Global Financial System (G10/BIS)
COBRI	Comité d’Organisation de la Banque des Règlements Internationaux (BIS Organisation Committee)
Comecon	Council for Mutual Economic Assistance
CPSS	Committee on Payment and Settlement Systems (G10/BIS)
EC	European Communities
ECA	Economic Co-operation Administration
ECSC	European Coal and Steel Community
EEC	European Economic Community
EMA	European Monetary Agreement
EMCF	European Monetary Co-operation Fund
EMS	European Monetary System
EMU	European Monetary Union
EPU	European Payments Union
ERP	European Recovery Program (Marshall Plan)
Euratom	European Atomic Energy Community
FOMC	Federal Open Market Committee (U.S. Federal Reserve)
FRBNY	Federal Reserve Bank of New York
G10	Group of Ten countries

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GAB	General Arrangements to Borrow (IMF/G10)
GATT	General Agreement on Tariffs and Trade
IBRD	International Bank for Reconstruction and Development (World Bank)
IADI	International Association of Deposit Insurers
IAIS	International Association of Insurance Supervisors
ICE	Independent Commission of Experts Switzerland – Second World War (Bergier Commission)
ICRC	International Committee of the Red Cross
IEPC	Agreement for Intra-European Payments and Compensations
ILO	International Labour Office
IMF	International Monetary Fund
IOSCO	International Organisation of Securities Commissions
MC	Markets Committee (G10/BIS)
MED	Monetary and Economic Department (BIS)
NATO	North-Atlantic Treaty Organisation
OEEC	Organisation for European Economic Co-operation
OECD	Organisation for Economic Co-operation and Development
RM	Reichsmarks
SDR	special drawing right (IMF)
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
UPU	Universal Postal Union
WP3	Working Party No. 3 (OECD)