Question 2. b) What were the objectives of Bretten woods system?

Solution: The key provisions of the Bretton Woods Agreement were as follows :

A new permanent institution, the International Monetary Fund (IMF), was to be established to promote consultation and collaboration on international monetary problems and to lend to member countries in need clue to recurring balance of payments deficits.

Each Fund member would establish, with the approval of the IMF, a par value for its currency and would undertake to maintain market exchange rates for its currency within one per cent of the declared par value.

Countries that freely bought and sold gold in international transactions were "deemed" to be adhering to the requirement that they maintain-the exchange rates within the one per cent margins. Thus the U.S.A., the only country that met this condition, was not expected to intervene in the foreign exchange market. Other countries would intervene by buying and selling the dollars against their own currencies, .to keep the rates within one per cent of their parities with the dollar.

Members would change their par values only after having secured the Fund approval. This approval would be given only if the country's balance of payments was in "fundamental disequilibrium". Exchange rate adjustment was not to be undertaken lightly. Temporary and cyclical imbalances were to be financed out of reserves or through borrowings from the Fund. Only a, long and continuous loss of reserve assets in support of an exchange rate would be evidence of this fundamental disequilibrium.

After a transitional period, currencies would be convertible i.e. countries would undertake to redeem balances of their currencies acquired by other members. Such convertibility would be either gold or the currency specified by the member requesting conversion.

Each IMF member country would pay into the IMF pool, a quota, one quarter of which would be in gold and the remainder in its own currency. The Fund would be. in a position to lend countries in deficit, out of its holdings of gold and other currencies arising from the subscriptions bf its members in relation to their quotas (to be determined according to each member's size in the world economy). But the Fund was not to lend to finance outflows of capital.

If a country's currency became 'scarce' in the Fund, the latter could authorise other countries to adopt exchange controls on imports and other current account purchases from the surplus country. (This sanction against countries in large surplus was offered by Americans in response to a charge by Keynes that the proposed system was asymmetrically severe to countries in deficit.)

FOR MORE NOTES VISIT http://eduspeaks.com/