

Are international organizations like the Bank for International Settlements unable to die?

A historical case study of the BIS

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Abstract International Organizations seem to be immortal or at least long-lived. In this paper several factors which may be responsible for this fact are put forward and then analyzed by studying the empirical case of the Bank for International Settlements (BIS), which has now survived for seventy-eight years all threats to its existence. This is the more surprising since it was heavily attacked by the government of the most powerful country of the world, the USA for some years. This country demanded the dissolution of the BIS at the Bretton Woods Conference in 1944 as a precondition for allowing nations to join the planned International Monetary Fund. Before this the Bank was also able to master the crisis resulting from the demise of the gold (exchange) standard and the end of the German reparation payments agreed on in the Dawes and Young Plans, both consequences of the Great Depression. The Bank even survived the events of the Second World War threatening it, and reacted creatively to the crisis posed by the founding of the European Monetary Union. It is shown that all suspected factors favoring the survival of international organizations were present in the case of the BIS.

Keywords BIS · Public choice · International organizations

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1 The Attack of the United States Against the Bank for International Settlements (BIS)

At the Bretton Woods Conference in July 1944 the following resolution was passed:

“The United Nations Monetary and Financial Conference recommends: The liquidation of the Bank for International Settlements at the earliest possible moment.”

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Behind this resolution stood according to the confidential report of a Swiss observer the American delegation headed by Harry White from the US Treasury who “*maintained a fanatical hatred against the BIS, since it had been mentioned by several quarters as the institute which could take the place of the [World] ‘Bank’*”. He stood behind the attack brought forward by the Norwegians in the commission [Commission III]: “*The proposal to liquidate the BIS in Basel put forward by the Norwegians of this commission led to a general surprise.*” (p.21)

“They [Harry White and his clique] also proposed during the discussion a new formulation with the content that no country could become a member of the ‘Fund’ [the IMF] as long as it maintained relationships with the BIS. This proposal was defeated by a majority after furious debates.

It will be scarcely possible, to stop the liquidation of the BIS, even if the Bretton Woods proposals should be rejected by the different parliaments, except if the whole net of bad rumors would be exposed by an energetic counter-attack.” (pp. 23 f.)¹

At a meeting of the Directorate of the Swiss National Bank (SNB) in July 1944 its President, Weber, asked whether he should not step down as President of the Verwaltungsrat (Board) of the BIS. He had assumed this position since it seemed to be advisable to the BIS to fill it with a personality from a neutral country during the war. But now Weber pointed out that according to reports in the press the liquidation of the BIS had been demanded at the Bretton Woods conference. But the other members of the directorate argued against such a step, as did the President of the Bankrat, the institution controlling the National Bank. However, the Directorate decided to also put the question to the Bankausschuss, the controlling subcommittee of the Bankrat.²

The Bankausschuss decided after a discussion that it would not be adequate for President Weber to withdraw from his position at the BIS.³

In spite of these violent attacks the BIS is still existing with widely extended activities, and in Summer 2007 the former President of the Deutsche Bundesbank, Hans Tietmeyer said that the survival of the BIS were more important than that of the IMF.⁴

2 General Reasons for the Survival of an International Organization

How could this miraculous rescue of the BIS occur against the intentions of the Treasury of the most powerful country of the world? Or is this just the most prominent example of an often observed fact, namely that public organizations, and specifically international organizations have a hard time to die? Since a discussion of the fate of the BIS may cast some light on this question, a short analysis may be adequate. But before turning to the specific reasons responsible for the survival and flourishing of the BIS it seems adequate to put together the factors which may be present or required to secure the survival of international organizations. Let me first

¹ Bosshard (1944), my translation from the German as of all later documents of the SNB.

² Minutes of the meetings of the Directorate of the Swiss National Bank No. 829, pp.923–924, July 27, 1944.

³ Minutes of the Bankausschuss, August 31/September 1, 1944, pp. 287–289.

⁴ Personal remark to the author in Summer 2007.

offer a list of the most important ones of the reasons favoring the survival of international organizations and then add a few comments.

List of Reasons favoring the survival of International Organizations

1. They are created by international treaties and can only be dissolved unanimously or by a majority of votes of the participating countries if provided in the treaty.
2. International organizations are only loosely controlled by the leading representatives of participating countries, not to speak of their budget decisions. For instance ministers or central bank governors can only sporadically pay attention to these organizations.
3. This strengthens the position of the permanent administration or board of the organization.
4. Members of the board have the same interest in maintaining the organization as its employees.
5. This interest is strengthened by special privileges, like freedom from taxes and diplomatic status usually granted by the founding treaty.
6. Politicians and central bankers may enjoy the regular meetings at the institution, its amenities and the chance to meet their counterparts in a relaxed atmosphere.
7. Persons belonging to these or similar groups may see a chance to later get a prestigious and well-paid job at such an organization.
8. The state and city where the organization is located have vested interests in its survival.
9. The same is true for countries and groups who are benefiting from its activities.
10. An international organization has the greater chances of survival the more broadly its tasks have been formulated in the founding treaty; and the more leeway this treaty leaves for changing them.
11. The chances of survival are also the greater the more an international organization is able to earn itself the means for financing its activities.

Public international organizations are in all cases created by international treaties. This fact already provides them with an advantage compared to national public organizations or agencies. Namely, they can be dissolved only by an agreement of several states. Even if the original treaty contains a clause that an international organization can be dissolved by a simple majority of participating states, this makes it still much more difficult to get rid of it than if just one government can take the decision. True, one or even some participating members may cut their financial contributions to the organization and thus try to starve it. But this may lead to critique or even to countermeasures by other participants. Even more, the organization may be successful in efforts to become financially independent, so that this avenue to influence or to abolish it may no longer be available.

The existence of any organization is threatened if the tasks for which it has been created are becoming unimportant or have even vanished. Thus the impressive development of international capital markets during the last decades has made the IMF ever less important, and it seems only to regain some of its earlier standing because of the deep international financial crisis beginning in 2008. Consequently two factors are of the greatest significance for the future survival of an international

organization. Namely first that the tasks assigned to it in the founding treaty are rather broad, and second that, if at all possible, it is granted the right to extend itself the domain of its activities.

Next, an international organization needs supporters strongly interested in its services, who are even prepared to assist it when attacked by strong opponents. This is obviously related to the range of its tasks and their usefulness to several groups. But that is not all. For support can also be won and maintained if the organization provides amenities and the hope of future prestigious or well-paid jobs to politically influential personalities. Let me illustrate this with one example. When the “Meltzer Committee,” which had to evaluate the workings of the international organizations for the US Congress some years ago, proposed to abolish the IMF and the World Bank, the US Treasury answered immediately with a statement rejecting their arguments and proposals.

In case of the BIS all the factors favoring the survival of international institutions were and are present, as we will see for the most important ones in the following sections.

3 Laying Sound Foundations for Future Survival

It is well-known that the BIS was originally founded to regularize the execution of the reparations inflicted on Germany by the Versailles Treaty and reduced by the Dawes Plan, approved by the governments in August 1924, and the Young Plan, signed in 1929. The latter led again to a substantial reduction of reparation payments “*in exchange for the commercialization of a major part of the reparations through the BIS*”, founded in February 1930.⁵ The committee who worked out the Plan, already revealed, in the competencies proposed for the BIS, the interests of the central banks of the participating countries to exclude all political influences and to extend the fields in which it could operate. In fact, central bankers had already for a long time striven to create a formal setting for central bank cooperation.

“In 1925, [Montagu] Norman [Governor of the Bank of England] first floated the idea of a central banks’ club, which was eventually reached with the creation of the BIS. *‘I rather hope,’* he wrote in September of that year, *‘that next summer we may be able to inaugurate a private and eclectic Central Banks’ ‘Club’, small at first, large in the future’*. [Benjamin] Strong [Governor of the Federal Reserve Bank of New York] soberly agreed that *‘a quiet meeting of some of the heads of the central banks’* might be useful.⁶

It seems also that the leading central bankers hoped to achieve more independence from their governments by creating a forum for their cooperation. Anyhow, they successfully used the occasion creating the BIS with the purpose to commercialize the problem of German reparations to realize this idea, as is clearly revealed by the following passages in the proposal of the experts which found their way into the treaty:

⁵ Toniolo (2005), p. 39. Toniolo provides a detailed discussion of these events and of the creation of the BIS.

⁶ Toniolo (2005), p. 30.

“The Board of Directors shall be made up in the following manner:

1. The Governor ... of the central bank of each of the seven countries to which members of the present committee belong, or his nominee, shall be director of the Bank *ex officio*. ...

The Directors shall elect a Chairman annually from among their own number. ...” (p. 63).

“The purpose of the Bank is to provide additional facilities for the international movement of funds, and to afford a ready instrument for promoting international financial relations. In connection with the German reparation annuities, it shall perform as trustee for the creditor countries the entire work of external administration of this Plan, ...” (p. 57)

“In particular, the Board of Directors [of the BIS]

1. shall have the right to adopt, modify, limit or extend the statutes of the Bank in such a manner as shall not be inconsistent with the provisions of the Plan, ...” (p.61).

“The Bank may in particular have the right

- a) to deal directly with central banks, or
- b) to deal through central banks which have agreed to act as its agent and correspondent, or
- c) to deal with banks, bankers, corporations and individuals in performing any authorized function, provided the central bank of that country does not enter objection. ...” (p.66).⁷

Already from this short sketch it is obvious that a firm base for the survival of the BIS had been created. First, since the central banks of the participating countries were strongly interested in this institution, where they could meet and cooperate outside of political influences; second, since the Directorate of the BIS was empowered to change its statutes on its own and third, since the BIS had the right to transact with all kinds of institutions in financial markets. In this way it was enabled to earn money and to be independent from outside financing. And since the governors of the central banks became the only directors of the BIS, they were in final control of it, were able to meet in a discreet atmosphere without political influences, to enjoy its amenities and were thus personally interested in its survival. Moreover, the Bank was protected by the international treaty creating it, so that it could only be abolished by a three quarters majority in the General Meeting.

4 Surviving the American Attack

It follows that central bankers had the greatest interest to prevent the dissolution of the BIS after 1944. Already during the war the German Reichsbank and the Banca d’Italia made clear that they were interested in keeping the BIS alive for the time

⁷ Sachverständigenausschuss (1929).

after the war.⁸ The Bank of England took a similar position: As Dr. Pfenninger reported from a visit at the Bank of England on November 27, 1939 to the Directorate of the Swiss National Bank (SNB):

“Sir Otto [Niemeyer, Director of the Bank of England, and Chairman of the Board of the BIS, 1937–1940] stressed that the BIS should be kept alive as an institution and with its present apparatus until the end of the war. It has to be expected that the return to a peace economy will lead to problems, and that for their solution the BIS can cooperate in one way or another. Though there exists today a great uncertainty about the nature of these later tasks, it is justified to assume that the Institute can provide services of great importance in rebuilding the economy.”⁹

And after the dissolution of the BIS had been demanded at the Bretton Woods’ Conference in 1944 it was stressed at a meeting of the Bankausschuss of the SNB:

“It is a wish of all central banks that the BIS will survive. It is true that the SNB would not have a special reason to oppose a possible abolishment of the BIS. But it is unpleasant for the managers of the BIS to be now under suspicion to have given preferential treatment to some belligerents; whereas the BIS has always striven to maintain a strictly neutral policy.”¹⁰

The same attitude was maintained after the end of the war by the Bank of England, but also the Federal Reserve Bank of New York though it was not a member of the BIS, and the central banks of the Netherlands, Belgium, France and soon Italy. By contrast, the strongest supporters of the dissolution were the governments, especially of the United States, led by Treasury Secretary Morgenthau and his Deputy, Harry White. Both hated the BIS because of its asserted role in favor of the Axis Powers; and also saw it as an obstacle for their plans for a new international monetary order with the IMF and the Bank for Reconstruction and Development as its pillars. But the members of governments changed and the central banks, especially the Bank of England succeeded in motivating their Treasuries to postpone the dissolution of the BIS for so long, until the political climate and the international monetary environment had changed enough that the governments were prepared to accept the further existence of the BIS. But this only after it had agreed in May 1948 to return 3740 kg of looted gold it had received during the war.¹¹

The support by the European central banks of the BIS can also be judged from the fact that its first General Meeting after the war on June 15/16 1947 was well attended by the governors of the member states.

⁸ Minutes of the Directorate of the Swiss National Bank [subsequently just “Minutes”], Nos. 903, p.1078, of October 26/27 1939 and 91, p. 108 of 5/6 February 1942.

⁹ Minutes, No. 18, January 12, 1940.

¹⁰ Minutes of the Bankausschuss SNB, August 31/September 1, pp. 288.

¹¹ Minutes, Nos. 892, July 24/25 and 1017, August 15, 1946. The Directorate of the SNB had advised the BIS not to do so, presumably because it wanted to prevent a precedent which might hurt the Bank. See also Toniolo (2005), p. 278.

“The coming together of the Governors of the most important European central banks offered the occasion to clarify in personal discussions several problems relating to Switzerland.”¹²

Change in climate and environment was, however, helped by the actions of the BIS itself. It had survived the war nearly intact and its expertise soon proved

“...useful to central banks for the execution of gold sales entailing forward repurchase and in exchanges of the yellow metal between markets, reducing physical transfers to a minimum.”¹³

Moreover, in

“November 1947, well before the Marshall Plan was enacted, an Agreement on Multilateral Monetary Compensation was signed by France, Italy and the Benelux countries. They designated the Bank for International Settlements (BIS) as the agent to which countries would report their bilateral balances each month.”¹⁴

It is characteristic, that the BIS and not the Bretton Woods institutions were seen as being capable to provide this service so important in moving back towards a multilateral system of exchange and international trade. Moreover, it is also important to note that the BIS took these activities in the face of a still threatening dissolution.

That the BIS took such activities is not surprising, for the members of each organization or institution have an interest in preserving its existence because of the income, prestige and reputation offered to them by it. But obviously there were also creative members present in the bank who put to good use their knowledge and competencies preserved during two decades of exchange controls and bilateralism.

With the services just mentioned, a precedent was set. When under American pressure the European Payments Union (EPU) was established within the framework of the Marshall Plan in 1950, to move Europe back towards multilateral and more liberalized trade, the BIS was again selected as the agent managing the payments system. And this against initial opposition by the IMF and the USA.¹⁵ As reported by the President of the Swiss National Bank from the meeting of the Board of the BIS on March 16, 1950:

“the creation of a new bank-like institution shall be prevented. The new administration shall be limited to a small committee (with secretariat), which decides the general rules for the administration of the “Payments Union”; all the technical services shall be managed by the BIS; ...”¹⁶

¹² Minutes, No. 817, June 19, 1947.

¹³ Toniolo (2005), p. 299.

¹⁴ Kaplan and Schleiminger (1989), p. 24.

¹⁵ Kaplan and Schleiminger (1989), pp. 38, 41 and 45. It is interesting that the Swiss delegation was instructed to support those countries who wanted to design the BIS and not a new institution to handle the payments system. Bernholz (2007), p.137.

¹⁶ Minutes, No. 272, March 16, 1950, p. 356.

Already in May 1947 the mood concerning the BIS had changed so much, that it could be ported to the Directorate of the SNB

“that Governor Frère [of the National Bank of Belgium], President of the Board [of the BIS], and Director General Auboin [of the BIS] had returned from Washington. According to their reports the Bretton Woods circles will no longer urge for a liquidation of the BIS. One seems to have recognized the importance of the BIS as a link among the European central banks. ... The legal position of the BIS shall not be changed. Her statutes remain unchanged.”¹⁷

And in December the Swiss National Bank noted that according to a report by President Frère

“The relationships [with the American authorities] are still overshadowed by the resolution agreed on in Bretton Woods. But Mr. Frère has the definite impression, that the American Treasury and the International Bank are wishing to cooperate with the BIS. Mr. Frère is convinced that no danger is threatening the BIS any longer from the American side and that there is no longer a question of its liquidation. It is planned to extend the already existing information service between World Bank and BIS.

Governor Sproul of the [New York] Federal Reserve Bank thinks that the efforts to further the balancing of financial payments between Italy, France, Belgium, the Netherlands and Luxembourg are of great psychological importance; he very much appreciated the use of the BIS for the technical performance of this service.”¹⁸

Still, it is revealing the deep hatred of American governmental institutions against the BIS that Japan was still required by the peace treaty with the USA of 1951 to leave the BIS.¹⁹ Today, of course, the Bank of Japan, is again a member of the BIS since long years.

5 The Crisis of the 1930s

The attack on the BIS by the American Treasury at the Bretton Woods Conference was not the only crisis survived by the BIS. In the following sections we will consider a number of other situations which have or could have brought the bank into difficulties or led it into crises which it had to survive. Such situations occurred when the gold (exchange) standard broke down and the payment of reparations by Germany ended in 1931 and thus made the original purpose of the bank obsolete, when the war among the countries which were represented on its board took place, when the European Payments Union was dissolved at the end of 1958, the Bretton Woods System broke down in 1971–1973, and when the European Monetary Union was created at the end of the century.

¹⁷ Minutes, No. 618, May 8, 1947.

¹⁸ Minutes, No. 1604, December 11, 1947, pp. 2285–86.

¹⁹ Minutes, No. 777, July 12, 1951, p. 884.

We begin by considering the measures taken by the BIS to survive the crisis created by the end of the gold (exchange) standard and the German payments servicing the Dawes and Young loans. Both these factors meant a sharp reduction of the activities and the income of the BIS (Fig. 1). Its net profits declined from 15.2 Swiss gold francs (with the gold content of the franc before its devaluation relative to gold in 1936) in 1931–1932 to 8.6 million in 1938–1939. The reasons for this development are obvious concerning the end of German payments, since the BIS lost the revenue from the fees for its service rendered in receiving the interest on the loans and in distributing it to the creditors in several countries. Moreover, they deprived the BIS of important sources of deposits. The reasons for the decline of revenues and profits are less obvious for those stemming from the breakdown of the gold standard. But central banks began soon after this event to convert their foreign exchange holdings with the BIS into gold, since to hold foreign currencies became risky because of the many devaluations following that of the British pound in the fall of 1931 as well as the foreign exchange controls instituted by more and more countries. The currency deposits with the BIS by central banks declined from 869 million gold francs in August 1931 to 132 million in 1938 and to 38.48 million in August 1939. Moreover, the activities of the Bank were now restricted by Art. 21 of its Statutes:²⁰

“The operations of the Bank for its own account shall only be carried out in currencies which in the opinion of the Board satisfy the practical requirements of the gold or gold exchange standard.”

What were the steps taken by Board and administration of the BIS to overcome this severe crisis? A first measure consisted in reducing the costs of its administration. They were cut from 4.218 million Swiss gold francs in 1931–1932 to 2.068 in 1938–1939.²¹ This was not possible without a reduction of salaries by 10% in the beginning of 1934 and by a further 6% in 1936. The staff was reduced from 115 in 1931 to 78 in 1934.²²

But second, this measure would not have been sufficient to prevent the bankruptcy of the BIS without still earning adequate, though reduced revenues. Several steps were taken to secure them. Fortunately for the Bank,

“a substantial proportion of the currency reserves held on deposit with the Bank were converted into gold by the depositors and the gold acquired was left with the Bank under earmark. This gold is not included in the monthly balance sheet...

Furthermore, .. the Bank has for the first time received deposits in metallic gold ... Full legal title to the gold deposited passes to the Bank ...”²³

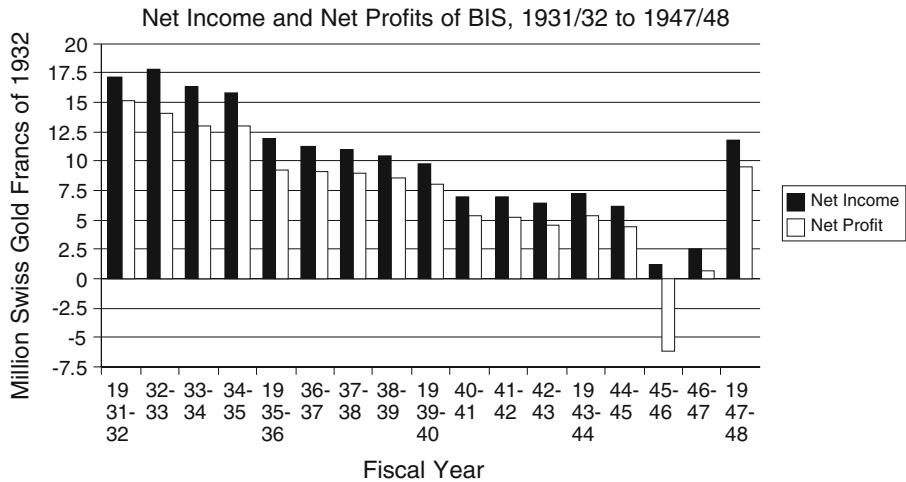
The latter deposits amounted to 28 million Swiss gold francs at the end of March 1934 and rose steadily during the following years. Moreover “...*the amount of gold earmarked has increased continually.*” It increased from 176 million Swiss gold francs on March 31, 1933 to 272 million on March 31, 1935. These deposits made it possible for central banks “*to avoid actual transfers of metal in opposite*

²⁰ Reprinted in Toniolo (2005), p. 638.

²¹ BIS: Monthly Reports for ends of years.

²² Toniolo (2005), p. 540 f., note 130.

²³ BIS (1934), p. 47.



Source: Monthly Reports of the BIS for Ends of Fiscal Years.

Fig 1 Net income and net profits of BIS, 1931/32 to 1947/48

directions...” In this way the BIS was able to earn fees by developing a kind of free international gold market among central banks and itself. It also undertook other gold operations for central banks, namely the buying, selling and transporting of gold. These activities were helped by the fact that the gold was held by the Bank in several locations, namely in London, New York and Berne.

Another measure taken by the BIS to secure its financial survival was the successful policy to encourage deposits of central banks in their own currencies to facilitate international trade settlements. For this purpose, since the gold standard had ended, the Bank also began to differentiate interest rates for several currencies from November 1933, so that it paid different rates for all deposits in different currencies in 1936. At the same time it made it a point to balance its assets and liabilities in the now inconvertible currencies or to secure them by agreements with central banks postulating that such deposits could be immediately converted at fixed rates into gold or convertible currencies (US dollars and Swiss francs). All these measures also allowed the BIS to circumvent the provisions of Article 21 of its Statutes mentioned above, which was adapted accordingly by the Board in 1936. Moreover, the Bank took great efforts to keep its investments as liquid as possible.²⁴

Given all these measures it is not surprising that Roger Auboin, at the time General Manager of the BIS, could conclude about two decades later:

“... the Bank was able, without any special difficulty, to pass through the recurrent periods of crisis in the years immediately before the Second World War— and this applies, in particular, to the critical days in September 1938, in March 1939 and then again in the summer of 1939.”²⁵

²⁴ For a fuller description see Toniolo (2005), PP. 185–189.

²⁵ Auboin (1955), p. 14.

But given the crisis threatening it, the BIS had, besides securing its financial survival, also to prove its usefulness especially for the member central banks which were its strongest supporters. The Bank was also encouraged to do so because of its remaining statutory task, central bank cooperation. For this purpose it increased its emphasis on information and research activities. The volume of its annual reports examining international and national financial developments increased from year to year. Country studies and comparative statistical analyses were added to the research agenda. This was widely appreciated by outsiders. Keynes wrote that the BIS

“...is now the leading authority for certain statistics, not easily obtainable ...It is particularly useful because it goes beyond the published statistics and ventures on certain estimates and opinions which can only be based on information not generally available ...”²⁶

Moreover, member central banks were invited to send expert staff to Basle to participate in the work of the Monetary and Economics Department for periods usually limited to two or three months. Thus the BIS became more and more a center of international financial diplomacy, helped by the remarkable competence of its staff. For this reason the meetings of the Board were also well attended by the Governors of the member central banks until the outbreak of the war.

6 The War Time Crisis

The outbreak of the Second World War threw the BIS into the worst crisis apart from that threatening it later because of the resolution taken at the Bretton Woods conference. Apart from the additional financial problems posed for its survival other dangers were more imminent because the Bank had been created by countries now mostly at war. Not only most of its Board members but also a large part of its staff came from nations now fighting each other. Only two of its Board members, the Governors of the Swedish and Swiss central banks came from countries remaining neutral during the whole war. The USA had never been a member of the BIS, though its President during the war, McKittrick, was an American. He had fortunately already been elected before the outbreak of the war as a successor of Johan Willem Beyen, a Dutchman, whose turn of office ended at the end of 1939. McKittrick arrived in Basel in December of this year. Unfortunately, he never was on good terms with the American Treasury.

We have already seen (Section 3) that the governors of the member central banks did not want to liquidate the BIS, which had thus to be kept neutral and quasi dormant during the war. The first major problem arose from the fact that the members of the Board coming from the warring countries could no longer attend its meetings. As the First Department reported to the Directorate of the SNB on January 12, 1940:

“Sir Otto Niemeyer, Chairman of the Board of the BIS, communicated orally the following messages to Dr. Pfenninger during his stay at the Bank of

²⁶ Quoted from Toniolo (2005), p. 194. The short sketch of these activities of the BIS is mainly based on Toniolo, pp. 191–195.

England on November 27, 1939. The meeting of the Board of the BIS which had been planned for October 9th could not take place because of the outbreak of the war. Since then Sir Otto has contacted several members of the Board of the BIS. This led to the result that the English and French members will not go by principle to Basel during the war; and that there will also be substantial difficulties for several neutral members to travel to Basel. This is especially true for Dr. Trips [from the central bank of the Netherlands] and the Japanese delegation.

The Board comprises presently 18 members, 8 of whom from countries at war. In their absence the necessary quorum of two thirds required by the Statutes will not be reached. It has been proposed that the nations at war transfer their authority to vote to members from the neutral countries. This solution, however, cannot satisfy, since this authority could always only be given for well defined cases which have been discussed before, ...²⁷

Finally, however, it was decided, after an exchange of many letters, that the day to day decisions should be taken by the management of the BIS, and that voting should take place at the General Annual Meetings by proxy given by the warring countries either to the President or to neutral Board members still able to travel to Basel. Moreover, it was decided to keep both the French General Manager, Auboin, and the German Assistant General Manager, Hechler, in office.²⁸

A next severe problem arose because the time in office of the President, McKittrick, would end on December 31, 1942. The situation became even more complicated when the Axis powers declared war on the USA in December 1941, so that the President of the BIS no longer belonged to a neutral country. It was clear that the political authorities in Germany and Italy would oppose the reelection of the national of an enemy state as President of the BIS. Especially the German Ministry of Foreign Affairs wanted either McKittrick to resign or to withdraw German membership in the BIS. It is interesting to note that in this sense Nazi Foreign Minister v. Ribbentrop and US Secretary of the Treasury Morgenthau shared a common dislike of the Bank.

The crisis was finally solved by following a suggestion made by McKittrick already in the beginning of 1941, and put forward somewhat changed by the governor of the Banca d'Italia, Azzolini: He proposed that the members of the Board of the BIS should elect the President of the SNB, Weber, as their chairman and that Weber would then reappoint McKittrick as President. This scheme was at first resisted especially in Germany, as already mentioned. But even in Britain Montague Norman, Director of the Bank of England first felt uneasy about the proposal, and the House of Commons debated whether it would not be better for the Bank of England to leave the BIS. But finally the Bank of England agreed, and in the end Emil Puhl, Executive Vice President of the German Reichsbank could overcome the objections of the Foreign Minister by arguing that the BIS had rendered Germany valuable services by allowing important gold and foreign exchange transactions providing the means of payment for the import of critical goods. This was a strong

²⁷ Minutes, No. 18, 12.1.1940.

²⁸ This paragraph is based on Toniolo (2005), pp. 213 f.

exaggeration, but obviously Puhl and other people of the Reichsbank wanted to preserve the BIS for the time after the war and German participation in the Bank.²⁹

The Swiss National Bank, too, agreed only reluctantly to the proposal. In a meeting of the Bankausschuss monitoring the SNB, its chairman reported:

The office of the Chairman of the Board of the BIS, formerly occupied by Sir Otto Niemeyer, London, has been vacant for some time [since the end of 1940]. It is now planned to elect a new chairman. Since the Board does not meet since the beginning of the war, the leading members have agreed in writing to propose President Weber [of the SNB] for being elected....

“The BIS is strongly interested in a quick election for the following reasons: The time in office of the present President, McKittrick does also expire at the end of this year. The member states represented on the Board of the BIS are now of the opinion that the President should be reelected. Only Germany has not yet answered definitely until today. Mr. McKittrick is an American so that one cannot expect that the representatives of the Axis countries officially agree to his reelection. The escape route which shall now be taken is as follows: The Chairman of the Board has to elect the President by proxy of the other members of the Board. The members of the Axis on the Board can then be satisfied with informally “taking note” of the election. A corresponding notification has already been given by the Italians and Japanese. With the German agreement can be reckoned soon, as I have been informed in writing by Director General Hechler [the leading German staff member of the BIS]. ...”

“Herr Weber is really not excited about the proposal. He has reserved his decision depending on the discussions by the banking authorities. He would like to make clear in this connection that the Bank for International Settlements has just been somewhat attacked in England....”

“The Bankausschuss agrees in principle that Herr Weber accepts the election as Chairman of the Board of the BIS. But it has to be sure that all members of the Board of the BIS declare in advance their agreement with the reelection of Herr McKittrick as President ...”³⁰

“The Chairman [of the Bankausschuss] reports that he has now received a letter from Director General Hechler in Basel telling him that now all relevant states, also including Germany, have deposited the wanted declaration ...

Herr Weber adds that he has been informed by Governor Rooth [of the Swedish central bank] that the agreements of the relevant countries have been obtained. He has asked Governor Rooth to send him photocopies of these declarations. It should be advisable to wait for these documents.”³¹

In this way this critical situation threatening the existence of the BIS had been finally solved, again with the help of all relevant central banks represented on the Board of the BIS.

Let us turn now to the financial plight of the BIS. Its net income and net profit shrunk even further compared to the difficult years before the war, and in 1945–1946

²⁹ Toniolo (2005), pp. 224–229.

³⁰ Minutes of the Bankausschuss of the SNB, No. 14, October 1, 1942.

³¹ Minutes of the Bankausschuss of the SNB, No. 15, October 29, 1942.

the Bank suffered the only loss in its long history (Fig. 1). Also, the Bank had to be careful not to violate in its financial transactions any of the restrictions imposed by belligerent and neutral countries. For this purpose in a declaration,

“...which was sent on 18th December 1939 to all the Bank’s correspondents, the Bank announced its express intention of refraining from all operations which, although permissible in a purely legal sense, were not ‘above reproach both from the point of view of belligerents and neutrals’;...”³²

The normal business of the BIS was further hindered when the USA even before its entrance into the war blocked all Swiss financial assets including those of the BIS in 1941, so that transactions were only allowed with special licenses of the treasury. This blocking of the Bank’s assets clearly violated its statutes, but as noted, the USA had not been a signatory of these agreements. Thus the Bank’s statements that it was not a Swiss institution were of no avail. The resulting problems were, however, mitigated in the beginning since the Federal Reserve Bank of New York helped to get a general license valid for many transactions. Later, however, the US Treasury withdrew this general license.

Still, the Bank was able to do some transactions with central and also to a limited degree with private banks. For instance, when

“...it was found, in the winter of 1939–1940, that the central banks of a number of countries not yet involved in the war desired to transfer a substantial part of their monetary reserves to places overseas (especially to New York), the BIS was able to handle a considerable part of these transfers. Moreover, certain central banks which had deposits at the BIS gave it a standing-order immediately to transfer these deposits overseas if their country became involved in the war. The arrangements thus made all worked out satisfactorily.”

And in spite of an ever more shrinking volume of transactions:

“Apart from the investments which the BIS had made in Germany in connection with the Hague Agreements- and these could obviously not be settled during the war- the Bank was able to realize and convert into assets with a high degree of liquidity all its old investments in other countries which had still been outstanding in 1939. Over the period 1939–1945 an amount equal to 120 million gold francs (about \$40 million) was in fact added to the Bank’s net holdings of liquid assets in dollars, Swiss francs and gold. The Bank had, on balance, suffered no financial loss: all the commitments which different central banks had entered into with the BIS had been scrupulously respected, notwithstanding the exceptional and unforeseeable circumstances which had prevailed in the years that had passed since the foundation of the Bank. At the same time, the deposits, as they stood in the books of the BIS on 1st September 1939, had been safeguarded in full, largely as a result of the protective measures which had been taken in good time by the Bank.”³³

³² Auboin (1955), p.14.

³³ Auboin (1955), p. 16.

Still, a specific problem arose since an ever higher percentage of the shrinking revenues of the BIS— 70% in 1940–1941, and towards the end of the war 82% — came from interest on the German investments, which the BIS had undertaken already in 1930–1931 in connection with the Dawes and Young agreements. They were meticulously transferred by the Reichsbank first in Swiss francs and later in gold, part of which came from sources looted by Germany during the war.³⁴ The BIS was aware of the latter problem and sought to justify the acceptance of the gold payments. As expressed later by the Belgian Roger Auboin, General Manager of the BIS from 1937–1958:

“It was not possible for the Bank, from a legal point of view, to refuse to receive any payments that were made in accordance with the contracts entered into under the Hague Agreements—and any such refusal would moreover have been prejudicial to the interests of the creditor countries, especially France and Great Britain. The BIS could not, however, rule out the possibility that, in spite of declarations to the contrary, the gold which was transferred might have been seized, in one form or another, in one of the occupied countries. After a careful examination of the questions involved, the Bank decided: (1) to accept gold in respect of all transfers legally due to it; and (2) to take steps to ensure that at some future date an enquiry could be made into the origin of all gold bars which it had received.”³⁵

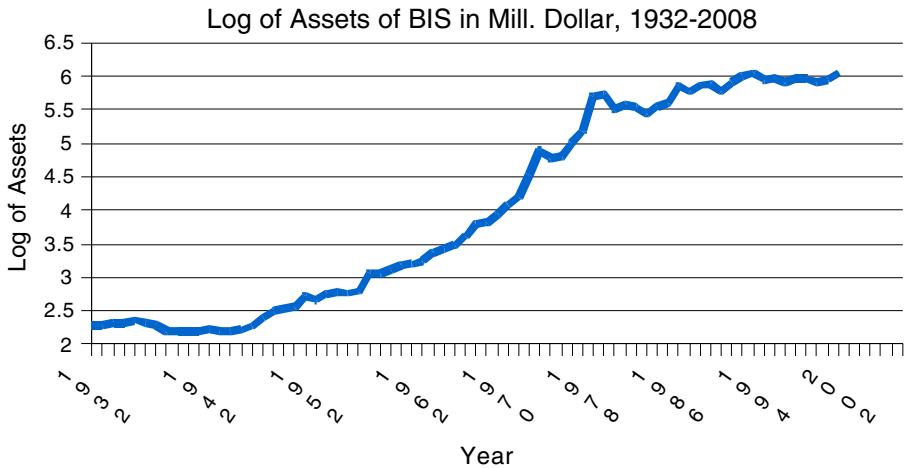
But it is clear that the BIS could not have survived the war financially without these German payments. Thus I am inclined to share Toniolo’s judgment that this risk was in fact incurred by the Bank to secure its survival. We have already noted that the BIS had to restore some of the gold after the war as one of the measures to escape the attack of the American Treasury started in Bretton Woods. But even in this case the BIS was later successful in being compensated for this loss by the Federal Republic of Germany.

7 The End of the European Payments Union and of the Bretton Woods System: Crises for the BIS?

It could be thought that the end of the European Payments Union in 1958 and the breakdown of the Bretton Woods System would have plunged the BIS into two other crises. But perhaps surprising for many observers this was not the case, as shown by Fig. 2. No negative developments of total assets can be observed for the years following these events. After a small drop from 552.9 million Swiss gold francs of 1932 in 1957–1958 to 540.22 1958–1959 they rose already to 612.68 million in 1959–1960.

³⁴ Toniolo (2005), p. 248.

³⁵ Auboin (1955), p. 16.



Source: Monthly Reports of the BIS for Ends of Fiscal Years.

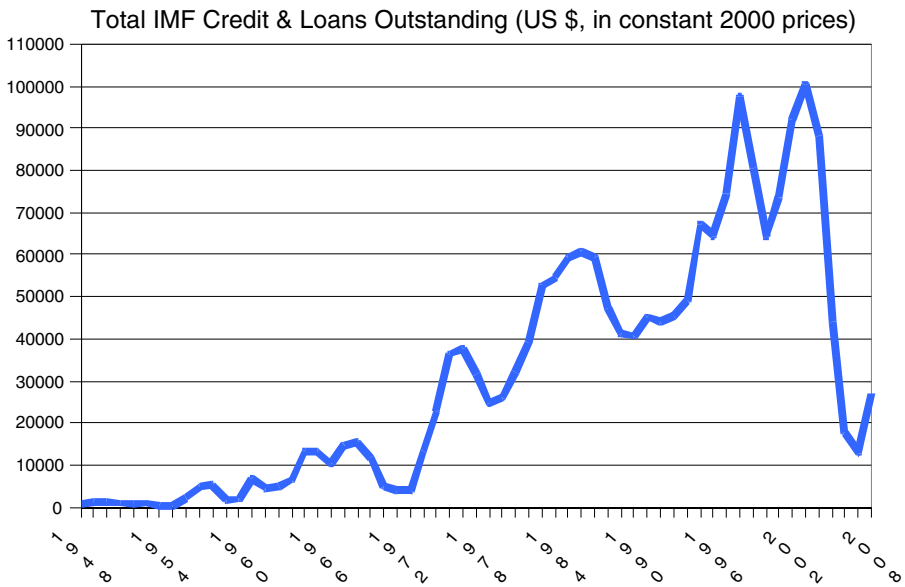
Fig 2 Log of assets of BIS in Mill. Dollar, 1932–2008

As expressed by Antonio d’Aroma, Secretary General of the BIS 1962–1974:

“The beginning of the sixties are in fact marked, after the return to convertibility, by a revival of the activities of the Bank, which had hibernated during the war, and afterwards slowly and cautiously retaken its role as bank of the central banks between 1945 and 1960; only from this moment it has not ceased to develop and increase the volume of its activities, following in a sense a geometric progression. It is sufficient to recall the evolution of its balance: 1.9 billion gold francs in 1931 (31.3.), 0.5 in 1946, 3.9 in 1961, 59.3 in 1978 ... One can bring together this revival of activities with the creation of the gold pool (October 1961) and with the first measures to support the British pound (March 1961), finally followed by the ‘general arrangements’ [to borrow] (1966, 1968 and 1977).”³⁶

Similarly positive developments occurred for the BIS after 1973. What were the reasons? To answer this question let us first remark that crises of the whole economy or the financial system need not necessarily be crises for international organizations. Quite the contrary, in certain cases such crises may even revitalize them since the help of these organizations is now thought for instance by governments to be needed to solve the crisis. That this is true can be seen by looking at the loans granted by the International Monetary Fund (IMF) (Fig. 3). As can be noticed, crises like the oil shock of 1973, the Mexican Debt Crisis of 1982, the fall of the USSR, the South East Asian Crisis and September 11, 2001 all helped the IMF to extend its financial activities. For in all these cases governments were prepared to increase the means available to it. But with the end of the crises the credits and loans of the IMF outstanding usually decreased. This was also the case when the Fed cut its Fund Rate to record lows in 2004. But then again, because of the financial crisis of 2008,

³⁶ D’Aroma (1980), p. 6., my translation from the French.



Notes: 1973: Oil Embargo; 1982: Mexican Debt Crisis;
 1991: Fall of the USSR; 1997: Asian Financial Crisis; 2001, Sept. 11;
 2004: Fed Funds Rate pushed to a record low of 1%.

Source: Data kindly transmitted by Steve Hanke, Johns Hopkins University.

Fig 3 Total IMF credit & loans outstanding (US \$, in constant 2000 prices)

the member states were prepared to increase its resources substantially. Thus it can be said that the survival of the IMF has been often furthered by crises, whereas the activities of the BIS were not dependent on them (Compare Figs. 2 and 3). True, the BIS has mostly played an important role in overcoming such crises, often by helping to coordinate speedy central bank assistance, but it has never done so by rising its capital through outside contributions. As already mentioned, the BIS has never been in need to call for new capital from its member states, but conducted its business by using its own earnings. Its original capital amounted to 500 million gold francs, of which only a quarter, 125 million was paid in by the participating countries. Its paid in capital was increased only to 300.7 million Swiss gold francs in 1971 and to 327 in 1999. It should be obvious that these facts imply greater independence of the BIS than of the IMF from central banks and especially governments.

But why did the activities of the BIS not shrink after its services for the European Payments Union ended with the dissolution of the latter and the move of its member states to full convertibility for foreign residents? A first reason was the balances, that is the claims and liabilities remaining among the members of the EPU after its dissolution, which had to be repaid in the years to come. Here again the BIS took the responsibility to technically assist in these financial operations. Second, the end of the EPU did not mean the end of financial crises. The first occurred when, after the first revaluation of the German mark and the Dutch guilder in March 1961, the

British pound came other pressure. This was soon followed by other crises, again of the pound, but also the French franc, the Italian lira and especially important, the US dollar. I cannot go into the details how the BIS was involved in trying to solve these crises apart from helping to bring together the relevant central bankers and to coordinate their actions. Among other measures a swap net among eight countries was created to help in emergencies with spot credits to be paid back after several months. As Max Iklé, then member of the Directorate of the Swiss National Bank, wrote in his memoirs:

In the course of the year [1962] Charly Coombs [of the Federal Reserve Bank of New York] constructed a swap net comprising eight countries and the BIS ... [with the BIS contributing 100 million \$ out of a total of 750 million].

The Bank for International Settlements (BIS) was included following our proposal [that is by Coombs and Iklé] into the swap net, since we believed this to be advantageous and since we saw the possibility of extending additional amounts of Swiss francs via the BIS.

This American swap net was more and more extended during the following years and reached an amount of 29760 million \$ in 1979, with the BIS contributing 1850 million. Fourteen countries were now included.³⁷

Naturally, this was only one side of the banking activities of the BIS. For

“In surveying the BIS’s business activities during the 1960s, it should be borne in mind that they were ... part and parcel of its functions as the center for central bank cooperation. ...banking activities were the executive branch of cooperation in such areas as lending amongst central banks, gold and currency swaps, syndicate loans, and the like. Some of these ... could not be carried out by other international financial organizations. The BIS was in an advantageous position because it could act swiftly, without formalities and in complete confidentiality, while at the same time remaining under the control of the central banks represented on the Board.”³⁸

This state of affairs was preserved after the breakdown of the Bretton Woods System. And in fact, there was no reason for a shrinking of the activities of the BIS. The BIS had already been active in the growing eurodollar market since the 1960s, and it played a prominent role in the recycling of petrodollars with the first oil crisis beginning in 1973:

“The II. Department informs [the Directorate of the SNB] that the monies stemming from the oil countries, which are offered in single parcels of 25 million dollars, are no longer seeking an investment for a few months but for maturities reaching from one to five years. If the inflow transcends one billion dollars, the BIS is unable to find for such maturities sufficient demand from first class commercial banks. She is asking whether these amounts could possibly be invested at the central banks belonging to it or with their governments.”³⁹

³⁷ Iklé, Max (Undated, after 1979): Erinnerungen. Zweiter Teil: Aus dem Berufsleben. Archive of the SNB, pp. 254 f.

³⁸ Toniolo (2005), p. 359.

³⁹ Minutes No. 513, June 13, 1974.

All the other banking activities of the BIS also continued to flourish. For instance:

“According to an information by the III. Department the investments in Swiss francs accepted by the BIS have risen from 7638 million francs to 7735 million francs in November 1974. The increase was namely caused by the growth of the deposits of other central banks and of international institutions by 179 to 3057 million...”

The BIS has of such deposits firmly invested 3807 million francs in foreign money markets.”⁴⁰

In conclusion we can state, that neither the dissolution of the European Payments Union nor the breakdown of the Bretton Woods System led to any crisis for the BIS. For whereas the IMF saw its original task removed by the latter event and had urgently to look for new tasks to survive, this was in no way the case for the BIS.

8 The Reaction of the BIS to the Founding of the European Monetary Union

The creation of the European Monetary Union has a long prehistory which began already soon after the foundation of the European Economic Community (EEC).⁴¹ Many plans were proposed and initiatives were taken. They led first to the creation of the Exchange Rate Mechanism, usually called the “Snake,” by the Basel agreement of April 1972, with the aim to preserve fixed exchange rates among the member states of the European Community in view of the awaited breakdown of the Bretton Woods System. The second step after the rather limited success of the Snake consisted in the foundation of the European Monetary System at the initiative of Helmut Schmidt and Giscard d’Estaing in 1979. The EMS had the same aim as the Snake but was buttressed by many more safeguards including massive mutual credit obligations in case of balance of payments problems of members.

It is interesting to note how the governors of the countries concerned reacted to several initiatives. When the Vice Chairman of the European Commission, Robert Marjolin, proposed a committee sitting in Brussels chaired by a member of the Commission and including the Governors of the six members of the EEC, this was flatly rejected by the governors meeting in Basel in November 1962. In May 1964 the EEC Council of Ministers finally approved the creation of a Committee of the Governors of the Central banks of the member states. The Commission got only the right to send an invited member to the meetings which were taking place not in Brussels but at the BIS in Basel. The secretariat of the Committee was provided by the BIS. Moreover, as already mentioned, the Snake was created by a “Basel agreement.” Finally, when the Delors Committee was set up to work out the blueprint for the European Monetary Union (EMU) in June 1988, it regularly met at the BIS in Basel, where it received secretarial help. All this shows the importance assigned by the central bankers to the BIS and their work in Basel.

In the end, however, the creation of the EMU necessarily led to a kind of crisis for the BIS. For now a part of the services provided by it to the central banks of the

⁴⁰ Minutes No. 1249, December 5, 1974.

⁴¹ Bernholz (1999), pp.737–788. See also Toniolo (2005), pp. 437–452.

EMU moved to the European Central Bank in Frankfurt. Many of the most important central banks supporting the BIS had become members of the System of European Central Banks and their governors met now regularly in Frankfurt. But the BIS swiftly reacted to these changes, mainly by extending its membership of central banks to several of the strongly developing countries of Eastern Europe, East Asia and Latin America. The membership reached a number of fifty-five central banks in 2006. China and Mexico are now represented on the Governing Board of the BIS by the Governors of the People's Bank of China and the Banco de Mexico⁴². Presently (2009) a Mexican, Jaime Caruana, is Director General of the BIS. Moreover, the Bank succeeded in establishing a branch in Hong Kong in 1998,⁴³ and afterwards another one in Mexico City. It follows that the success of the BIS to overcome all adversities depended mainly on its capability to provide services wanted by central banks and central bankers and the international financial community. The title of Toniolo's book *Central Bank Cooperation at the Bank for International Settlements, 1930–1973*, is revealing in this respect, for it was written for the BIS at the occasion of its 75th anniversary in 2005.⁴⁴ Finally, the BIS has been always protected, as mentioned above, by its well-designed statutes and its capability to finance itself by its own earnings without any government contributions.

Over the decades the BIS has also steadily extended the range of its services for her clients. A full description of the nature and scope of these services would be far too extensive to describe in this paper. But its activities can be summarized under four headings:

1. the BIS operating as a banker to central banks;
2. as a forum for international monetary and financial cooperation
3. as a center for monetary and economic research;
4. as a participant in international crisis management.⁴⁵

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⁴² BIS (2006), pp. 213 and 215.

⁴³ BIS (1999).

⁴⁴ See also the volume presenting the papers of a conference at the occasion of this anniversary: Borio et al. (eds.) (2008).

⁴⁵ For a detailed description of the astonishing range of the BIS's activities see Bernholz (2000).

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