

Preserving the Dollar for the Casino Rejecting the Substitution Account

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Submitted: July 31, 2025 – Accepted: November 4, 2025 – Published: March 31, 2026

Abstract

This essay re-examines the story of the 1978 proposal for a substitution account, an instrument to solve the dollar overhang and enhance the role of Special Drawing Rights introduced by the International Monetary Fund. Beyond its value as a failed attempt to reform the international monetary system, the demise of this initiative highlights the U.S. difficulties in cooling the “casino capitalism” of the late 1970s: from the shortcomings of the multilateralism of the Carter Administration, to the objective of preserving the dollar privilege, to the struggle of conjugating the agency of multiple governmental institutions.

Keywords: Carter Administration; international monetary system; Multilateralism; Federal Reserve; Substitution account; IMF.

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1 Introduction

In the mid-1970s the international monetary system was in a state of precarious equilibrium. After the decision of the U.S. President Richard Nixon to suspend gold-dollar convertibility in 1971, the members of the International Monetary Fund (IMF) had struggled to find an agreement on the future of the system, particularly when it came to exchange rates. The role of gold, of the dollar and of the relatively new Special Drawing Rights (SDRs) had been much debated, but the discussions had left many aspects unclear.¹ The reform process that had followed 1971, resulting in the amending of the IMF Articles of Agreement, was heavily criticised: commentators defined it as a non-reform, whose final outcome left the exchange rate regime “completely up in the air.”²

The unsatisfactory reform had taken place at a difficult time for the U.S. economy, which was transitioning from the flourishing post-war years of the 50s and 60s to the stagflation of the 70s. The stagnating economy was well represented by the slow-down of productivity and the swings in the GDP growth rate, which had gone from 5.6% in 1973 to 0.5% the following year due to the added repercussions of the oil crisis.³ Just as concerning was the unemployment rate, which increased from 1973 to 1975 and then again from 1979 to 1982, reaching 9.7%.⁴

Besides the recession there was, of course, inflation, which was affecting not only the U.S. but also the rest of the world, due to the special status of the dollar. The increase in welfare and social spending of the 60s promoted by the Lyndon B. Johnson Administration, as well as the increase in military spending to fund the Vietnam war efforts, were crucial factors in growing the amount of dollars in circulation. Just as detrimental was the expansionary monetary policy promoted by Arthur Burns, Nixon’s appointee to the role of Chairman of the Federal Reserve, who succumbed to political pressures that wanted him to prioritize having high employment rather than low inflation. Consequently, by the mid-70s, the international community faced the so-called “dollar overhang,” a phenomenon characterized by an excessive amount of dollars in circulation and in countries’ reserves, which caused frequent depreciations of the currency.

Devising a solution without a proper reform of the international monetary system seemed unlikely. With the status of the dollar as the world’s reserve currency slowly eroding and inflation showing no signs of abating,⁵ countries started to consider other solutions, such as diversifying their foreign exchange reserves. The procedure might have reduced the risk of putting all the eggs in the dollar basket, but it was also frowned upon by West Germany and Japan, which were wary of the possible internationalization of their currencies.⁶

Within Western Europe, there was also talk about increasing cooperation. The end of Bretton Woods, the lack of exchange rate stability and the weakening of the dollar were some of the factors that brought the European Economic Community (EEC) forward in their discussion of European monetary cooperation, a process which started in 1970 with the Werner Plan and eventually led to the

1. Barry J. Eichengreen, *Globalizing Capital: A History of the International Monetary System*, 2nd ed. (Princeton University Press, 2008); Barry J. Eichengreen, *Exorbitant Privilege: The Rise and Fall of the Dollar* (Oxford University Press, 2011); Margaret Garritsen De Vries, *The IMF in a Changing World: 1945-85* (International Monetary Fund, 1986).

2. Tom De Vries, “Jamaica, or the Non-Reform of the International Monetary System,” *Foreign Affairs* 54, no. 3 (1976): 586, <https://doi.org/10.2307/20039595>. In the years since the reform, other historians would come to this conclusion: see for example Harold James’s notion of “nonsystem” in Harold James, *International Monetary Cooperation Since Bretton Woods* (Oxford University Press, 1996), 228–59.

3. “GDP growth (annual %) - United States,” World Bank Open Data, accessed December 19, 2025, <https://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG?end=2024&locations=US&start=1961>.

4. “Unemployment, total (% of total labor force) (national estimate) - United States,” World Bank Open Data, accessed December 19, 2025, <https://data.worldbank.org/indicator/SL.UEM.TOTL.NE.ZS?end=2019&locations=US&start=1960&view=chart>.

5. “Inflation, consumer prices for the United States,” Federal Reserve Economic Data, accessed July 12, 2025, <https://fred.stlouisfed.org/series/FPCPITOTLZGUSA#/-:text=Inflation%20as%20measured%20by%20the,specified%20intervals%2C%20such%20as%20yearly>.

6. Joanne Gowa, “Hegemons, IOs, and Markets: The Case of the Substitution Account,” *International Organization* 38, no. 4 (1984): 664, <https://doi.org/10.1017/S0020818300026904>; James M. Boughton, *Silent Revolution: The International Monetary Fund 1979-1989* (International Monetary Fund, 2001), 837.

establishment of the European Monetary System (EMS) in 1979.⁷ The system, designed to restore stable exchange rates among EEC member countries, had them committing to keeping their rates within a certain margin of an artificially created European Currency Unit. Nevertheless, the EMS could not overcome the dependency of the EEC, and of the international community at large, on the U.S. dollar and particularly on its role as a reserve asset.

It is within this context of economic hardship and monetary instability that then Director of the IMF Johannes Witteveen brought up the idea of a substitution account at the meeting of the IMF Interim Committee in Mexico City on April 30, 1978.⁸ The concept behind it was simple: it was an account, administered by the IMF, that allowed its members to swap out a reserve asset in exchange for another. In this case countries would be able to deposit their abundant dollar holdings and obtain in exchange SDR-denominated claims.⁹ This would not only gradually diminish the so-called “dollar overhang,” but also lower the risk of countries being affected by further depreciations of the dollar.¹⁰

This was not the first time a concept similar to the substitution account had been brought up in international monetary discussions, but previous proposals had not gone very far and neither did this last scheme. Despite the 1978 version being the closest the account ever came to its implementation, on April 25, 1980, the Interim Committee meeting in Hamburg surprisingly decided to cast it aside.¹¹ The idea would never be picked up again.

In re-examining this proposal and its demise, this essay seeks to go beyond the narrative of the substitution account as a paragraph in the larger chapter on the attempts to reform the international monetary system of the late 70s. Rather, it adopts the point of view of the Administration of the U.S. President Jimmy Carter in evaluating the proposal according to its possible effects on the dollar. The substitution account thus becomes an excellent example of two concurring processes. On the one hand, the slow erosion of Carter’s aptitude towards multilateral cooperation stemming from the U.S. government’s inability to put systemic equilibrium before the “exorbitant privilege” of its currency. On the other, the unchecked acceleration towards the casino-like capitalist system that was first described by Susan Strange in 1986.¹²

Renown British journalist and political economist, Susan Strange devoted an entire book, *Casino Capitalism*, to the analogy describing the Western financial system as a casino where instead of playing roulette or blackjack, the gamblers deal in bonds and government securities.¹³ According to her analysis, the gradual transformation of the system into a casino overlaps with a fifteen-year period which has witnessed two concurring processes: the strengthening of financial markets and the weakening of national governments.¹⁴

Strange cited the substitution account precisely in the last chapter of the book, titled “Cooling the casino,” expanding on how the global issue of the stabilization of the financial system could only find an answer in the action of national governments, the U.S. among all others.¹⁵ However, the case study of the failure of the substitution account highlights how, even if there were the willingness to prioritize the stabilization of the system as opposed to the casino, governmental agency is hindered by

7. Emmanuel Mourlon-Druol, *A Europe Made of Money: The Emergence of the European Monetary System* (Cornell University Press, 2016); Duccio Basosi, “Principle or Power? Jimmy Carter’s Ambivalent Endorsement of the European Monetary System, 1977–1979,” *Journal of Transatlantic Studies* 8, no. 1 (2010): 6–18, <https://doi.org/10.1080/14794010903533875>.

8. International Monetary Fund, *International Monetary Fund Annual Report 1978. Annual Report of the Executive Board* (International Monetary Fund, 1978), 139–40, <https://doi.org/10.5089/9781616351908.011>.

9. Boughton, *Silent Revolution*, 939.

10. Dieter Gehrman, “No Solution for International Monetary Problems,” *Intereconomics* 15, no. 3 (1980): 113, <https://doi.org/10.1007/BF02924348>.

11. Paul Lewis, “Dollar Plan for IMF is Shelved,” *New York Times*, April 25, 1980, <https://www.nytimes.com/1980/04/25/archives/dollar-plan-for-imf-is-shelved-finance-chiefs-unable-to-agree-on.html>.

12. Susan Strange, *Casino Capitalism* (Blackwell, 1986).

13. *Ibid.*, 1–2.

14. *Ibid.*, 17–20.

15. *Ibid.*, 142.

the division of power into the legislative and executive branches and the central bank, which respond to different logics, some more devoted to financial capitalism than others.

To retell the tale of this substitution account in this way, the paper will tackle first and foremost the Carter Administration's aptitude towards multilateral cooperation and the hidden struggles within this strategy. This is a fundamental starting point, as historical literature has identified in the difficulty of finding a global agreement regarding the financial balance of the account one of the key elements that led to the failure of the proposal. Specifically, the stalemate that developed between the United States and the other members of the Group of 5 (G5)—the United Kingdom, France, Japan and West Germany—made it impossible to bring the proposal forward.¹⁶

Secondly, the paper will describe how the opinion of the Administration regarding the substitution account evolved over time. Taking evidence from primary sources pertaining to the Department of the Treasury and the National Security Council (NSC), it will depict the inversely proportional relation between the support for the account and the strength of the U.S. currency, highlighting just how much the role of the dollar influenced the considerations of the government on the account.

Lastly, the paper will look at the concurring agencies of two institutions separate from the executive—Congress and the Federal Reserve System—to explain how both the need to seek congressional approval and the tightening of U.S. monetary policy from October 1979 onwards were decisive in determining the failure of the substitution account.¹⁷

2 A Weak Basis for Multilateralism

Upon his death in late 2024, prominent international newspapers were flooded with articles reflecting on the life and times of former U.S. President Jimmy Carter.¹⁸ Despite his presidency lasting only one term, his four years in office—coupled with more than forty years of post-presidential activism—firmly painted the image of Carter as a peacemaker and a strong advocate for human rights. From the Panama Canal Treaties to the Camp David Accords, his legacy speaks of solid morals and a great disposition towards international cooperation, which was far from a given for U.S. Presidents when he was elected in 1977.¹⁹ This collaborative disposition within the realm of foreign policy took a triangular shape specifically when it came to dealing with the international political economy, which in the late 1970s was mainly concerned with stagflation.

The origins of the triangular shape must be traced back to Carter's little national political experience before the presidency. Having been a nuclear engineer in the Navy, a businessman, and then Governor of his home state Georgia, when he got to the Presidency he still lacked experience in foreign policy and was, as stated by both himself and by commentators, an outsider in Washington.²⁰ This shortcoming had brought him to place experienced Washington insiders in key foreign policy roles, for instance by appointing Zbigniew Brzezinski as National Security Advisor. Brzezinski, who would go on to dictate the foreign relations of the Carter Administration until the end of its term, was the one who had first invited Carter to become a member of the Trilateral Commission, the non-governmental organization promoting a closer cooperation between the U.S., Japan and Western Europe that he had founded in 1973 together with investment banker David Rockefeller. Twenty mem-

16. Gowa, "Hegemons, IOs, and Markets," 672–76; Robert N. McCauley and Catherine R. Schenk, "Reforming the International Monetary System in the 1970s and 2000s: Would a Special Drawing Right Substitution Account Have Worked?," *International Finance* 18, no. 2 (2015): 194–95, <https://doi.org/10.1111/infi.12069>.

17. Peter B. Kenen, "Reforming the Global Reserve Regime: The Role of a Substitution Account," *International Finance* 13, no. 1 (2010): 1, <https://doi.org/10.1111/j.1468-2362.2010.01259.x>; Gowa, "Hegemons, IOs, and Markets," 666–76; Boughton, *Silent Revolution*, 943.

18. Chris McGreal, "From Panama to Palestine, Jimmy Carter Refused to Let His Moral Voice Be Silenced," *The Guardian*, December 30, 2024, <https://www.theguardian.com/us-news/2024/dec/30/jimmy-carter-foreign-policy->; Peter Baker et al., "Jimmy Carter, Peacemaking President Amid Crises, Is Dead at 100," *The New York Times*, December 29, 2024, <https://www.nytimes.com/2024/12/29/us/politics/jimmy-carter-dead.html>.

19. Sean Wilentz, *The Age of Reagan: A History, 1974–2008* (Harper Perennial, 2009), 16–25.

20. Betty Glad, *An Outsider in the White House: Jimmy Carter, His Advisors, and the Making of American Foreign Policy* (Cornell University Press, 2009); Wilentz, *The Age of Reagan*.

bers of the Commission eventually became part of the Carter Administration—most notably, besides Brzezinski, were Secretary of State Cyrus Vance and Secretary of Defense Harold Brown—and thus shaped the strategy of Carter’s foreign policy. Distancing himself from the bipolar Cold War framework that had characterized his predecessors, especially in the first couple of years of his presidency, Carter and his government adopted a more comprehensive view of global politics, recognizing the need for a North-South dialogue and the reality of economic interdependence.²¹ Moreover, within the economic context, the Commission planted the seed for the new trilateral strategy: a stronger coordination of economic policies between the U.S., Western Europe and Japan, that could facilitate a relaunch of the global economy.²²

In 1977 this idea of trilateralism took practical form in the proposal for the delivery of a joint stimulus package by the United States, Japan and West Germany—the so called “three locomotives.” The plan entailed the simultaneous adoption of expansionary policies that could generate new growth in the stagnant economies. As it was strongly linked to the concept of economic interdependence, the joint stimulus has been defined as “the brainchild of the OECD and the Trilateral Commission,”²³ but it did not initially capture the enthusiasm of the Japanese and German leadership and, even when it was implemented later down the line, offered disappointing results compared to what had been too optimistic projections.²⁴ This was perhaps the first clue that the trilateral strategy the Carter Administration had subscribed to would be hard to pursue.

The more narrowly monetary domain also offered other clues that the administration’s practice of trilateralism—or multilateralism even—was feebler than its preaching, due to the special role of the dollar as the main world reserve currency which the U.S. was reluctant to give up. An example of this phenomenon is Carter’s ambivalent opinion on the aforementioned European Monetary System. Despite the initiative not posing a threat to the hegemony of the dollar, Carter’s endorsement was contingent on the effects of the EMS on the U.S. currency and he gave his approval only after the European Economic Community had answered his concerns regarding the system.²⁵

The substitution account also fits within this narrative. During the initial development of the initiative by the IMF staff, it was clear that the U.S. held many doubts on the project and preferred to focus its efforts on tackling inflation.²⁶ The Undersecretary of the Treasury for Monetary Affairs Anthony Solomon had declared himself “very leery of this proposal” and admitted there were several systemic implications that needed to be further analyzed before an endorsement.²⁷

One of the most contentious points of the initiative, which the historiography portrays as a primary factor in determining its demise, was the financial balance of the account.²⁸ Simulations run by the IMF and U.S. government predicted that the account would accumulate a deficit of twenty percent of its SDR liabilities after thirty years. This raised concerns about the financial insolvency of the account and called for a remedy.²⁹ The U.S. endorsed the option of selling IMF gold reserves and

21. Kristin L. Ahlberg, “Trilateralism,” in *A Companion to Gerald R. Ford and Jimmy Carter*, ed. Scott Kaufman (John Wiley & Sons, Ltd, 2015), <https://doi.org/10.1002/9781118907634.ch17>.

22. E. Stanly Godbold Jr., “From Plains to Atlanta, 1924–1974,” in *A Companion to Gerald R. Ford and Jimmy Carter*, 68, <https://doi.org/10.1002/9781118907634.ch4>.

23. Judith Stein, *Pivotal Decade: How the United States Traded Factories for Finance in the Seventies* (Yale University Press, 2010), 158–59.

24. W. Carl Biven, *Jimmy Carter’s Economy: Policy in an Age of Limits* (University of North Carolina Press, 2002), 145–51.

25. Basosi, “Principle or Power?”; Biven, *Jimmy Carter’s Economy*, 166–68.

26. Michael Blumenthal, “Information memorandum from Secretary of the Treasury Blumenthal to President Carter,” March 24, 1978, *Foreign Relations of the United States, 1977–1980, Volume III, Foreign Economic Policy*, ed. Kathleen B. Rasmussen (Government Printing Office, 2013), (hereafter FRUS), Document 123, <https://history.state.gov/historicaldocuments/frus1977-80v03>.

27. Anthony Solomon, “Briefing Memorandum from the Under Secretary of the Treasury for Monetary Affairs (Solomon) to Secretary of the Treasury Blumenthal,” April 12, 1978, FRUS.

28. Gowa, “Hegemons, IOs, and Markets,” 671–73; McCauley and Schenk, “Reforming the International Monetary System in the 1970s and 2000s,” 196–200.

29. “Substitution Account – Calculation of the interest rate to be paid on SDR-denominated claims,” SM/79/283, December 10, 1979 IMF Archives, 4, <https://archivesscatalog.imf.org/Details/ArchiveExecutive/125020741>; “Report of the Executive

using the profit to pay out the insolvency, de facto dumping the responsibility onto the actions of the Fund.³⁰ On the other hand, Western European countries and Japan were afraid that an only-gold back-up would leave free rein to the U.S. to adopt policies that further depreciated the dollar, possibly exacerbating the problem. As a matter of fact, this solution guaranteed the U.S. the possibility of maintaining an autonomous monetary policy and introduced no real constraint to limit their money supply.³¹ In the eyes of Japan and Western Europe, a hybrid solution that relied on more than just gold profits to finance the potential shortfall was the preferred option. But negotiating a third alternative became impossible.

The U.S. camp was extremely reluctant to compromise on anything other than the gold-only solution. They attempted to persuade their European and Japanese allies of this option in January 1980 during a G5 Summit, but did not succeed.³² This produced a stalemate in the discussions that eventually led the U.S. to withdraw its support for the initiative before the Interim Committee meeting held on April 25, 1980.

The faith of these negotiations and the failure of the substitution account paint a picture of the Carter Administration in contrast with the one that campaigned for a concerted effort to relaunch the economy: uncooperative with the allies they originally wanted to devise a joint stimulus package with, set in their ways not just in the broad IMF setting but even in the smaller and supposedly more effective forum of the G5. This case highlights the discrepancy between the professed multilateralism of the United States and their unwillingness to compromise. The question then shifts to the reasons for the emergence of this discrepancy. Diving deeper into the causes of this mismatch can help us go further in the analysis of the vision of the American government for the international monetary system, which was revolving mainly around the status of the dollar.

3 Alleviating the Pressure on the Dollar

Between the initial skepticism shown by Undersecretary Solomon in April 1978 and the progress the proposal for a substitution account had made by 1980 stands a fundamental element of this story: the change of attitude of the Carter Administration regarding the account. This change of attitude and the willingness of the U.S. government to consider and discuss an initiative that could partly modify the international monetary system is a complex matter to judge. While it could be taken as proof of a greater disposition towards multilateral cooperation, it more accurately reveals itself as the result of an evolving strategy for the dollar, which guided the reasoning of the Administration above all other factors. The primary sources of the Administration, and particularly of the National Security Council, are the key to interpreting this matter.

When first introduced, the political implication behind the proposal for the substitution account was quite clear. The initiative had a double objective in enhancing the role of the SDRs and in counteracting the dangerous diversification of countries' reserves into multiple currencies,³³ but these two goals were born out of the same problem: the weakness of the dollar. The endorsement by the Carter administration of an initiative that promoted the usage of an alternative reserve currency and that in some way acknowledged the decline of the dollar, might have been taken as a sign that the administration itself expected a further decline or was unable to take adequate measures to resolve the issues the dollar was facing at the time.

Board to the Interim Committee on a Substitution Account," SM/80/89 Revision 1, April 11, 1980, IMF Archives, <https://archivescatalog.imf.org/Details/ArchiveExecutive/125019771>.

30. Gowa, "Hegemons, IOs, and Markets," 674.

31. McCauley and Schenk, "Reforming the International Monetary System in the 1970s and 2000s," 198.

32. Boughton, *Silent Revolution*, 942; Gowa, "Hegemons, IOs, and Markets," 672.

33. "The Chairman's Summing Up of the Discussion on the Review of the Question of a Substitution Account and Related Issues Executive Board Meeting 79/25 – February 12, 1979," BUFF/79/38, February 14, 1979, IMF Archives, <https://archivescatalog.imf.org/Details/ArchiveExecutive/125023244>.

Particularly, the relation between the dollar crisis and national security did not escape the attention of the NSC Staff, which was concerned with the possibility that the weakness of the dollar could spread to the reputation of the United States as a whole. In April 1978, the Staff explicitly stated their worries:

If we are seen as not having the resolve and expertness to take the steps necessary to strengthen the dollar, some foreigners may well be asking themselves whether we have the resoluteness and mastery to shape even more complex and hazardous situations. Some foreigners may pose the question to themselves this way: Can a country that has not been able to prevent its currency from tumbling be relied on to act decisively and effectively to influence events far from its shores?³⁴

If the strength—or weakness—of the dollar might affect the perception of the international community of U.S. power and of the ability to preserve it, endorsing an initiative like the substitution account did not seem like a smart strategy. On the contrary, it might look like the U.S. was handing over some degree of its monetary hegemony. But a change came in the first half of 1979, as the reality of the instability of the dollar started to loom larger.

While the administration was trying to prevent more depreciations of the dollar with their anti-inflation plan, there had been a growing interest in the role of SDRs among IMF members, and the momentum for the proposal had built up among the international community. It is likely that, in this context, the Carter administration started to see the substitution account and the promotion of the SDR as a more viable option: an opportunity to alleviate the pressure on the dollar, without compromising its role as primary currency.

While in February 1979 the judgement on the proposal was that it promised “only marginal benefits to the international monetary system and could be costly for the U.S.,”³⁵ there was a real turnaround in the following months as the inflation rate reached double digits. On April 9, 1979, Special Representative for economic summits Henry Owen wrote to National Security Advisor Brzezinski a list of goals for foreign economic policy, the last of which was continuing negotiations on substitution account.³⁶ The topic had thus officially entered the agenda of issues the administration intended to keep discussing, seeing it as a chance to transfer to the SDRs some of the burdens that were weighing down the dollar and to restore a more advantageous position for the U.S. currency.

A poignant piece of evidence that attests to this intention is the assessment of the advantages and disadvantages of the dollar’s position discussed in a weekly report of the NSC that Advisor Brzezinski addressed to President Carter on May 3, 1979. In the document, Brzezinski went so far as suggesting studying an alternative pricing of oil that was based on a basket of currencies rather than on the dollar:

Mike was against even studying proposals to convert oil pricing to a ‘basket of currencies,’ for fear that this would show lack of confidence in the dollar and lead to an even heavier speculation. Now that we are past the crisis, I think we should face this issue squarely. I believe it is very unwise to continue to accept a substantive economic disadvantage just to keep up appearances. Great Britain drove its economy into the ground in a futile effort to maintain the prestige of sterling as a reserve currency.³⁷

The comparison with Great Britain and the discussion of oil prices are a testament to the significance of the discussion. The Administration was questioning whether the very elements that gave the dollar its privileged status were worth keeping or rather if they had turned into responsibilities they might want to get rid of.

34. “Paper prepared by the National Security Council Staff,” undated, FRUS, Document 128.

35. Robert Hormats, “Briefing memorandum from the acting Assistant Secretary of State for Economic and Business Affairs (Hormats) to the Under Secretary of State for Economic Affairs (Cooper),” February 8, 1979, FRUS, Document 198.

36. Henry Owen, “Memorandum from the Special Representative for Economic Summits (Owen) to the President’s Assistant for National Security Affairs (Brzezinski),” April 9, 1979, FRUS, Document 207.

37. Zbigniew Brzezinski, “Memorandum from the President’s Assistant for National Security Affairs (Brzezinski) to President Carter,” May 3, 1979, FRUS, Document 213. The “Mike” Brzezinski is referring to is the Secretary of the Treasury at the time, W. Michael Blumenthal.

In the summer of 1979, the health of the dollar deteriorated even more as President Carter was facing the energy crisis. At that point, the substitution account might have sounded like just what the doctor ordered. In the aftermath of the infamous “malaise speech,”³⁸ of the cabinet changes and of the new rounds of depreciation for the American currency, the interest of the U.S. on the substitution account solidified up to the point of Undersecretary Solomon expressed “the definitive statement of U.S. support” for the initiative.³⁹

This evolution of the U.S. attitude showcases that, despite the substitution account being proposed as a way stabilize the international monetary system, it was not examined by the Carter Administration as a cooperative or multilateral effort, but rather always as an initiative that would have an impact on the dollar and thus needed to be evaluated first and foremost according to the advantages it might bring to the U.S. currency.

4 Intra-Governmental Struggles

While the objective of alleviating pressure on the dollar acts as a key to analyzing the shift between the initial skepticism of the Administration for the substitution account and the endorsement of the proposal in mid-1979, understanding why the U.S. then went from being willing to negotiate the initiative to withdrawing its support in April 1980 requires a step further.

The concept of the U.S. government being concerned about the burdens and advantages of the dollar and taking decisions based on currency trends is correct but also at the same time too simplistic, as it presents the U.S. government as a monolithic entity with a single opinion. To fully understand the demise of the substitution account, the government must be looked at in its entirety, appreciating the concept that the systems of checks and balances between the executive and legislative branches complicated any strategy that the Carter Administration might have preferred.

This was the case for the substitution account as well. The opinion of the legislative branch became an issue due to the legislative implications required to implement the proposal and to the likelihood of obtaining the necessary votes in the U.S. Congress to do so. The fundamental node in this case was, once again, the financial balance of the account. A congressional authorization would have been sufficient to approve the account in case of the adoption of the gold-only solution to finance the possible insolvency of the account. However, if the IMF members countries were to agree on a different option that required additional financial backing from the United States, the administration would have needed Congress to pass an appropriation bill, explicitly allocating funding to the initiative. This might have been much harder to achieve.⁴⁰

The U.S. Congress was not completely hostile to the idea of a substitution account, but neither was it enthusiastic. Two congressmen, Representative Henry S. Reuss and Senator Jacob Javits, had urged the Carter Administration to consider the proposal in 1979.⁴¹ However, the limited success of previous proposals to reform the international monetary system and the other difficulties that the Administration had encountered when dealing with Congress up until that point indicated that the odds were not in their favor.⁴²

Explicit clues of this preoccupation regarding Congress can be found in the documents of the Carter Administration as well. In a memorandum dated February 1980, Secretary of the Treasury William Miller suggested that accepting to pay a supplement on the interest rate to ensure the long-term financial balance of the account was impossible for the U.S., it “could trigger Congressional crit-

38. Kevin Mattson, *What the Heck Are You Up To, Mr. President?: Jimmy Carter, America's "Malaise", and the Speech That Should Have Changed the Country* (Bloomsbury Pub Plc USA, 2010).

39. Boughton, *Silent Revolution*, 940.

40. Gowa, “Hegemons, IOs, and Markets,” 674.

41. Gowa, “Hegemons, IOs, and Markets,” 675. We know that the Administration had taken into account their suggestion as the news is reported as well in S. Y. Cross. “Memorandum from the U.S. Executive Director to the Under Secretary Solomon,” February 5, 1979, FRUS, Document 194.

42. For more on the relationship between Carter and Congress, see Kaufman, *A Companion*, 379–409.

icism and efforts to curtail the Secretary of the Treasury's authority to determine interest payable on the public debt" and lastly it was also "unnecessary given the availability of IMF gold."⁴³

Miller agreed that the aim of the United States should be endorsing the gold-only solution, not expressing its willingness to take more responsibility and pay a higher interest rate on the account. He was confident in the fact that, when developing these recommendations for the proposal, Undersecretary Solomon had kept periodic consultations with the members of the Senate and the House Banking Committee, which were "supportive of both the broad principle and the specific U.S. negotiating objectives."⁴⁴

Having spoken with Congress, the executive went on to pursue a solution that aligned with the principles shared by the committees involved in the discussion, the one they believed was politically possible to achieve at domestic level. But when a different preference started to emerge among other IMF member countries and the G5 pushed for an option regarding the financial viability of the account that the administration knew would be unacceptable for Congress, negotiating a deal seemed impossible.

Looking back to that time in a 1983 interview, Fred Bergsten, who had been the Assistant Secretary of the Treasury for International Affairs in the Carter Administration, would sum it up:

We'd have to tell Congress that we'd have to put up at least a contingent liability that could run into untold billions—who knows?—in order to reduce the role of our own currency in the world. And that sounded like a hard sell [...] a long shot.⁴⁵

It did not make sense for the Treasury to keep pursuing a proposal they knew would not be approved by Congress. As such, the delicate balance between executive and legislative powers impeded the course of the negotiations. Political scientist Joanne Gowa went as far as writing that "neither pressure exerted by private-sector interests nor bureaucratic politics played as important a role in defining the U.S. position on the financial balance issue as did the division of power between Congress and the Executive."⁴⁶

To the dynamic between the Carter Administration and the U.S. Congress we must also add a third element: the Federal Reserve System (Fed), an entity whose simultaneously private and public nature increases the complexity of this case. As its Board of Governors constitutes a federal government agency, the Federal Reserve is granted its authority by and must report to the U.S. Congress; the governors must be appointed by the President and go through Senate approval before taking on their role. Nevertheless, the bank does not require any authorization from either the legislative or executive branch on how to conduct monetary policy and reach its goals of maximum employment and stable prices. As a consequence, whether to consider the actions of the Federal Reserve as an exogenous or endogenous factor in the tale of the substitution account is up for debate. What is undisputed is that U.S. monetary policy developments must have been a decisive factor in the fate of the proposal as they directly impacted the dollar, even more so as the end of the 1970s featured one of the most relevant watershed moments in U.S. monetary policy history: the Volcker shock.

On October 6, 1979, the Chairman of the Federal Reserve Paul Volcker announced a new anti-inflation plan designed to fight inflation and bolster the dollar by issuing new restrictive targets for the U.S. money supply, a decision that had as primary effect a spike in the federal funds interest rate.⁴⁷ It is within the realm of possibility that Volcker's decision to take such strong measures against inflation was partly prompted by the talks he had in Europe in the context of the Interim Committee meeting of the International Monetary Fund held a few days earlier in Belgrade to discuss also the substitution account. Looking at the succession between these events brings back the matter of multilateralism and the ambiguous attitude of the U.S. on international monetary cooperation.

43. William Miller, "Memorandum from Secretary of the Treasury Miller," February 28, 1980, FRUS, Document 233.

44. *Ibid.*, 233.

45. Gowa, "Hegemons, Ios, and Markets," 675. The interview with Fred Bergsten that Gowa writes about was done on March 14, 1983.

46. *Ibid.*, 675.

47. Steven Ratiner, "Anti-Inflation Plan by Federal Reserve Increases Key Rate," *New York Times*, October 7, 1979, 1, 35.

Before the IMF meeting in Belgrade there had been another sharp depreciation of the dollar, which prompted the U.S. to look for a closer cooperation with Germany on the matter of monetary policy in attempt to stabilize the market.⁴⁸ On September 29, 1979, Secretary Miller and Chairman Volcker had met in Hamburg with German Chancellor Helmut Schmidt and their foreign counterparts, the Head of the Deutsche Bundesbank and the German Minister of Finance, with the purpose of discussing monetary relations and of finding an agreement on the necessity to keep pursuing the initiative of the substitution account.⁴⁹ Then came the meeting in Belgrade, an important step for the proposal. With the account gaining consensus and the U.S. giving its approval, the Research Department of the IMF agreed to develop a new outline of the account. The only thing left between the proposal and its approval was finalizing a scheme for its financial balance that could be satisfying for the required majority of IMF members.

It is impossible to pinpoint exactly to what degree the bilateral with the German delegation and the talks in Belgrade influenced the opinion of Paul Volcker on the future of the dollar, but it is puzzling that the Chairman flew back to Washington before the Interim Committee meeting was even over. Following his return, he acted quickly to devise and get approval on a new anti-inflation plan. On October 4, 1979, Federal Reserve staff members were already sharing with the rest of the Federal Open Market Committee (FOMC) a memorandum on possible new reserve targeting procedures for the money supply prepared upon Volcker's request.⁵⁰ A conference call followed on October 5, and then on October 6 the FOMC officially chose a new strategy to handle the U.S. monetary policy and thus tackle inflation.

Primary sources offer little help in interpreting the Fed's decision. From the transcript of the October FOMC meeting emerges Volcker's skepticism for a joint dollar support package, but the impressions that the Chairman had gathered in Europe regarding the attitude of foreign countries were left off the record, with the secretary stopping the recording during Volcker's assessment of his recent international meetings.⁵¹ The IMF and the SDR, on the other hand, were barely mentioned; but the failure to discuss them might be a clue in itself. It is not unplausible to assume that Volcker gained a better understanding of the stance of the dollar during those international meetings, leading him to believe that neither the substitution account nor an international dollar support package could be enough in the fight against inflation. The perception that international cooperation would not be enough to rescue the dollar thus could have played a part in the Fed choosing a tougher and self-reliant anti-inflation strategy.

After the "Volcker shock," in December 1979, when writing to the President about the upcoming decisions the administration had to prepare for in the G7 Summit scheduled for June 1980, Henry Owen underlined the fact that the strength of the dollar was necessary to maintain a strong bargaining power when negotiating the conditions of the substitution account.⁵² But perhaps it had gained too much strength. As the currency began to finally appreciate again in early 1980, the interest in the substitution account declined accordingly.⁵³ At the beginning of April, the Italian newspapers *Il Corriere della Sera* speculated on how the newfound strength of the U.S. currency was messing up the plans of those who sought to reform the international monetary system and stated that there was a common feeling that the interest of the U.S. for the substitution account was rapidly depleting now

48. William Miller, "Memorandum from Secretary of the Treasury Miller to President Carter," September 26, 1979, FRUS, Document 227.

49. This is reported in a note in Miller, "Memorandum from Secretary of the Treasury Miller to President Carter," September 26, 1979; as well as in John Vinocur, "Countries Agree to Bolster Dollar," *New York Times*, September 30, 1979, 13.

50. "FOMC Meeting Presentation Materials," October 4, 1979, Federal Reserve, <https://www.federalreserve.gov/monetarypolicy/files/FOMC19791005material.pdf>.

51. "Meeting of Federal Open Market Committee," October 6, 1979, Federal Reserve, <https://www.federalreserve.gov/monetarypolicy/files/FOMC19791006meeting.pdf>, 9.

52. Henry Owen, "Memorandum from the Special Representative for Economic Summits (Owen) to President Carter," December 18, 1979, FRUS, Document 229.

53. Kenen, "Reforming the Global Reserve Regime," 1; Boughton, *Silent Revolution*, 943; Gowa, "Hegemons, IOs, and Markets," 678–79.

that the dollar was recovering.⁵⁴ With the campaign against inflation guided by Volcker, the urgency over the approval of the substitution account had evaporated. Considering this context, the decision of the U.S. to withdraw its support for the initiative before the Interim Committee meeting of April 1980 does not seem so surprising.

5 Conclusion

The story of the substitution account did not end in 1980. In November 2009, in the wake of the global financial crisis, the former Assistant Secretary of the Treasury Fred Bergsten wrote a paper suggesting that a substitution account could help countries exchange unwanted dollars, as well as “reduce the risk of future market disruptions and contribute to an increased role for SDRs.”⁵⁵ Despite Bergsten not being the only one calling for the adoption of such an instrument,⁵⁶ the idea never gained enough momentum to be seriously considered. However, the endorsement of the account by Bergsten thirty years after the failure of the 1978 proposal corroborates the idea that the withdrawal of U.S. support from the initiative in 1980 should not be attributed to the unfavourable opinion of the American Treasury. The initiative was not judged based on its merits as a possible reform of the international monetary system, but on different considerations.

The impossibility of finding an agreement with the other G5 members on how to finance the potential shortfall of the account worsened the likelihood of it being approved and reduced the willingness of the United States to engage in further negotiations. Moreover, the evidence presented before showcases how, despite the emphasis on cooperation and the disposition towards multilateralism, when it came to the international monetary system the Carter Administration was guided mainly by another concern: the preservation of the privilege of the dollar. The substitution account was thus seen primarily as an additional helpful instrument that could alleviate some of the burdens faced by the U.S. currency—but only if it was implemented at the most favourable conditions acceptable to Congress or in case the Federal Reserve failed to resolve the “dollar overhang” with its own restrictive monetary policy.

In the end, the “slam on the monetary brakes,”⁵⁷ and the solution to the stagflation of the 1970s, came from the Volcker shock rather than from the substitution account. But the resulting increase in the federal funds rate was so abrupt that it cannot be considered as a successful attempt to control the “casino”—on the contrary, it created more economic uncertainty in the early 80s. Looking beyond this timeframe, the resurgence of the idea of the substitution account after the 2008 crisis corroborates the warning that Susan Strange issued at the end of her *magnum opus*: in the twenty-first century, as the consequences of financial gambling become more severe, the global community is still looking for a way to cool the casino.

54. “Pandolfi affronta il ‘ricatto’ del dollaro,” *Il Corriere della Sera*, April 4, 1980. In Italian, “La forza del dollaro è in grado forse di scombinare i piani agli economisti incaricati di vegliare sulla programmazione [...] mette in pericolo i piani dei grandi strateghi della riforma del sistema monetario internazionale [...]. Si ha la sensazione netta che almeno da parte americana questo interesse stia scemando rapidamente ora che il dollaro è di nuovo forte.”

55. Fred Bergsten, “The Dollar and the Deficits: How Washington Can Prevent the Next Crisis,” *Foreign Affairs* 88, no. 6 (2009), 27.

56. Kenen, “Reforming the Global Reserve Regime,” 4–9.

57. Strange, *Casino Capitalism*, 160.