Working papers

Dollarization Diplomacy:US Policy Toward Latin America Coming Full Circle?

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Beginning in 1999, US policymakers suddenly began to show an interest in the idea of encouraging Latin American countries to adopt the US dollar. A bill was even introduced into US Congress that would allow the US Treasury to share seigniorage revenue with foreign governments that chose this course. Those with a long historical memory might find this new US interest in "exporting the dollar" to Latin America strikingly familiar. Between 1900-1915, US policymakers devoted considerable energy to the task of encouraging the use of the dollar within Latin American monetary systems. Indeed, by the end of this period, the leading US financial advisor to Latin America - Edwin Kemmerer - was even calling for the creation of a monetary union based on the dollar to involve all of the Americas.

Is the new US interest in Latin American "dollarization" stemming from the same causes as in the past? And why did the US interest in promoting dollarization abroad wane after the First World War never to resurface again until the last few years? This paper addresses these questions in an effort to place current initiatives in the longer historical context of US-Latin American monetary relations in the 20th century. To date, there has been remarkably analysis of this kind.[1] This neglect is unfortunate because, as I show in this paper, the history of US policy towards Latin American dollarization has changed in very interesting and dramatic ways over the past one hundred years. After examining US efforts to promote dollarization in the first two decades of the 20th century, I show how these efforts not only waned after World War One but were in fact soon reversed. During the 1940s and 1950s, US policymakers set out deliberately to undo the work of their predecessors by encouraging many Latin American governments to de-dollarize their monetary systems.

In the final section of the paper, I examine the ways in which this history helps us to understand the politics of US policymaking in this area during the current period. I argue that an examination of these changing directions in US policy not only provides a useful historical backdrop for contemporary debates. It can also help us identify key factors that influence US international monetary policymaking in this area. Economists have so far dominated discussions about the idea of the US promoting dollarization in Latin America. To explain current developments, however, more attention needs to be given to the political factors influencing US debates on the issue. Through an analysis of the history of US policy, I hope to contribute to this task in ways that complement the work of some other scholars who have begun working on this topic (Cohen forthcoming, Schuldt 2000).

The Role of the Dollar in the "Dollar Diplomacy" of the Early 20th Century

US policymakers first became interested in promoting the dollar's use in Latin America during the early 20th century when their country was suddenly expanding its military and economic influence across Central America and the Caribbean. The US military expansion in the region began with its acquisition of Puerto Rico as a colony in 1898 and the creation of protectorates in Cuba and Panama a few years later. Within the next two decades, US also intervened militarily at various times in countries such as the Dominican Republic, Haiti, and Nicaragua to establish and maintain "customs receiverships". During this period, US trade and investment relations with this region also

expanded dramatically. Indeed, during the Taft Presidency (1909-1912), American policymakers began to talk widely about how US influence would be more effectively achieved in the region through the "dollar diplomacy" of US trade and investment instead of military means.

The monetary dimensions of US policy in this period have received less attention within scholarly literature than other policies relating to trade, investment and military intervention. The work of Emily Rosenberg (1985, 1999) on US "gold standard diplomacy", however, provides an exception. She shows how, beginning around 1900, the US started to encourage foreign countries to adopt gold exchange standards based on national currency units that were identical to that of the dollar. This policy was shaped heavily by liberal economists - especially Charles Conant, Jeremiah Jenks, and Edwin Kemmerer - whose belief in the gold standard's scientific virtues dovetailed with imperial ideologies of the time that the US was bringing "progress" and "modern civilization" to the region. In their view, the gold standard would bring monetary stability, an objective that was not just a virtuous goal in and of itself. It also would lay the foundation for economic growth by fostering the confidence of foreign investors and encouraging the growth of domestic savings and financial markets.

The policy also served specific US interests. US policymakers hoped that American businesses would find transactions with the region much simpler once stable gold-based currencies were established abroad similar to that which existed in the US. If countries created national currency units that were identical to the US dollar, US businesses might also gain a special competitive edge over their European competitors. In addition, when countries adopted a gold-exchange standard, they were encouraged by US advisers to hold their gold balances in New York, a move that bolstered New York's status as a regional financial center. In Rosenberg's (1999: 24) words, a key goal was to "create a gold dollar bloc, centered in New York, to rival the *de facto* sterling standard". US financial interests also often benefited from gold standard diplomacy because they were called upon to provide the loans for monetary stabilization programs. And finally, in regions where the US had established colonial administrations, US officials hoped that the creation of a stable exchange rate vis-à-vis the dollar would simplify public sector payments to and from the home country.

Encouraging foreign countries to adopt a currency unit whose value was identical to the dollar was not the same as asking them to use the dollar within their domestic monetary systems. In practice, however, US policymakers and business also encouraged the latter practice in many of the countries where they had influence. In these contexts, "dollar diplomacy" involved the promotion not just of trade and investment but of the dollar itself, a practice that we might call "dollarization diplomacy". With the exception of Puerto Rico (noted below), however, US policymakers did not do what they are debating today; that is, encourage the dollar to be adopted as the exclusive currency of foreign countries. Instead, they simply pressed for it to be used alongside the national currency abroad.

From a US perspective, this practice would reinforce the benefits already outlined. It promised to facilitate US economic interactions with Latin America still further by eliminating currency-related transaction costs altogether. It could also provide US businesses with more of a competitive edge vis-a-vis foreign competition because of their familiarity with the dollar as well as its availability to them. The widespread

circulation of dollars within a foreign monetary system would also provide a further guarantee of that country's stable exchange rate and domestic price stability.[2] As I note below, US policy in this area was also associated by some with ideologies of imperialism at the time as well as Pan-Americanism.

The US first showed an interest in promoting the use of the dollar in Latin America in Puerto Rico soon after the island was colonized. At the time of colonization, Puerto Rico had its own currency based on a fiduciary standard that Spanish colonial authorities had introduced only three years earlier. With the US arrival, the dollar quickly began to circulate alongside the local currency because it was used by US troops. This soon created confusion since the exchange rate between the dollar and the local currency differed from place to place and initial attempts to fix the exchange rate proved hard to enforce. In this context, US officials soon decided to replace the Puerto Rican currency with a monetary system based on the US dollar (Kemmerer 1916a: 169-209, 228-33). The currency changeover was generally supported by the local business community who saw it as a way to bolster exports to the US. But it quickly generated controversy with others when many businesses used the opportunity to alter wages and prices in ways that were disadvantageous to workers and the poor. Workers' strikes soon spread throughout the island, strikes that were ended only when businesses agreed to adjust wages upwards (Kemmerer 1916a: 217; Rosenberg 1999: 13-14).

Indeed, so strong was the opposition in Puerto Rico to monetary reform that it helped discourage US policymakers from introducing the dollar into the Philippines, the other colony acquired at the time. Some Congressmen favored the introduction of the dollar there on the grounds that it was part of the US imperialist mission; as one politician put it, the dollar would "teach [the Filipino] the lessons of the flag and impress upon hum the power and glory of the Republic" (quoted in Kemmerer 1916a: 303). But US officials worried about a repeat of the Puerto Rican experience in a context where opposition to the US colonial rule was already strong. As one US advisor noted, the introduction of the dollar "would lead to frequent exploitation of the ignorant, too much bickering, and to criticism and suspicion of the American authorities" (Kemmerer 1916a: 303). Instead, they replaced the Spanish colonial monetary system with a new distinctive colonial peso currency in 1903 that was based on a gold-exchange standard.[3]

When Panama became a US protectorate independent from Colombia in 1903, the issue of encouraging the US dollar's use abroad was raised once again. Because most US workers in the US-controlled Canal zone were to be paid in gold dollar coins, US policymakers wanted Panama's monetary system to be linked closely to the dollar. The US government also favored the link because it would soon be importing large amounts of equipment for the canal construction. If Panama's monetary system remained on a silver standard whose value was declining at the time, the cost of these imports would be constantly rising (Rosenberg 1999: 19). But US officials stopped short of pushing for the adoption of the dollar as an exclusive currency, as they had in Puerto Rico. Instead, in an agreement reached in 1904, the US supported the decision of Panama to introduce a new national monetary unit (the balboa) with silver peso coins based on a gold-exchange standard that would replace the Colombian coin in the country. Indeed, they agreed that this money would be legal tender not just in the country but in the US-controlled Canal Zone too. At the same time, however, they demanded that the value of the new unit be

identical to that of the US gold dollar and that US gold coins be made legal tender throughout the country.

In this way, a dual currency system was created in the country involving the use of both dollars and Panamanian currency, an arrangement that paralleled the quasi-sovereign nature of the country's protectorate status. Interestingly, the dual currency system also quickly became an integral part of the country's labor regime. In the Canal Zone, US administrators paid most US employees in US gold currency, while reserving the use of Panamanian silver pesos for the wages of most other workers from Panama and the West Indies. This distinction between those on the "gold roll" and those on the "silver roll" symbolized a stark economic division in the labour force, with the former receiving much more generous wages and benefits. As Conniff (1992: 78) notes, the system "quickly became a means of racial segregation as well, wherein gold meant white and silver non-white", a segregation that extended even to the use of such things as toilets (Major 1993: ch.4, 9). After World War One, US currency came to dominate the monetary system because most Panamanian silver coins had been melted down or exported during the war (McCain, 1965: 109; Grigore 1972, Stickney 1971, Rosenberg 1985, 185-6). But the labels "silver" and "gold" workers remained in place until 1948 (when they were replaced by terms "US rate" and "local rate" - Major 1993: 220).

The US also encouraged the dollar to be used alongside local currency in its new protectorate of Cuba. At the turn of the century, Cuba in fact had no distinctive local currency; its monetary system was made up of a heterogeneous mix of Spanish and French gold and silver coins whose values fluctuated vis-à-vis each other according to their metallic context and changes in the world market prices for these metals. Initially, the US simply set a fixed exchange rate of the dollar against the Spanish and French gold coins. They refrained from trying to introduce a gold exchange standard partly because of Cuban fears that a US-directed monetary reform might be a prelude for colonization. US business interests in the sugar sector also favored the existing monetary system because they paid their workers in the depreciating silver coin while receiving profits in gold-based currency. (Rosenberg 1999: 20). In the years leading up to 1914, however, the dollar was increasingly used alongside the existing currencies, particularly in payments to the government and in sectors tied to foreign trade (Wallich 1950: 32).

In 1914, the Cuban government finally established its own distinctive gold-based currency in response to growing nationalist sentiments as well as to the widespread local desire to reduce the heterogeneous nature of the monetary system. Although the old French and Spanish coins were withdrawn from circulation and lost their legal tender status, the government refrained from doing the same to the US dollar because of the nature of Cuba's political and economic relationship with the US (Wallich 1950: 33). As in Panama, the gold content of the new Cuban peso was also set at the same rate as that of the dollar. This move was designed by the government to make local bookkeeping easier and to strengthen the acceptance of the new peso, but it also had the effect of tying the Cuban monetary system even more closely to that of the US. Throughout the 1920s, this tie became closer still when the dollar became the dominant currency in circulation. In the wake of a financial crisis in 1920-1 that wiped out most of the Cuban-owned banking sector, the US Federal Reserve Bank of Atlanta (as well as that of Boston between 1923-6) even established an agency in Cuba to carry out limited central banking activities such as lender of last resort functions (Wallich 1950: 69).

The US dollar also began to circulate widely alongside national currencies in some other Central American and Caribbean countries where the US had an increasingly dominant economic and political presence in the early 20th century.[4] One of these was the Dominican Republic where the US had intervened military in 1904 in order to control its customs collection. At the time, the Dominican republic relied primarily on various foreign coins for its monetary system. A devastating depreciation of its currency in 1890s had eroded confidence in locally-issued money. Upon assuming control of the country, the US pressured the government to adopt a gold-exchange standard based on a national currency unit that was equivalent to the dollar. In the absence of a locally-issued currency, this reform had the effect of encouraging the US dollar to become the only currency in the country, a situation that then lasted until 1937 when some Dominican subsidiary coins were issued (Wallich and Triffin 1953: 10)

Another important and interesting case was Honduras. US advocates of dollar diplomacy had developed a plan for Honduras to introduce a gold exchange standard in 1911, but the plan had been abandoned when it was rejected by US Congress (Rosenberg 1999: 65-66).[5] Despite this, the US dollar became the key currency in the Northern region of country where US banana companies dominated the economy. The banana plantations were enclave economies with few linkages to the rest of the country; inputs were mostly imported and their workers - mostly from the West Indies - were paid in dollars which were then spent on imported goods sold in company stories. In this context, a kind of dual currency system quickly emerged in the country that was not based on class as in Panama, but on geography. The banana-producing zones used a monetary system based on dollars, while the rest of the country employed the national silver currency, (Vinelli 1950, Bulmer-Thomas 1987: 30, Rosenberg 1999: 108-9, Young 1925: ch.9; Weaver 1994: 91-92).

It is worth noting that the US did not always encourage dollars to be used in countries within this region where it had influence. In the case of Haiti, for example, it initially strongly opposed the practice. Because Haiti did not produce its own gold coin, US gold coins were already widely used in the country before the US intervened militarily in the country in 1915 (Kemmerer 1916b: 78fn2). The Haitian government had committed itself to stabilize its currency in 1910 as part of a French-led foreign loan package, but the reform had been delayed because of its disagreement with the foreign-controlled National Bank that was supposed to issue the new currency (Munro 1964: 374-7). After the US assumed control of the country, the monetary reform was finally undertaken in 1919 and it included a provision declaring the gourde and the dollar to be legal tender. Interestingly, however, Moore notes that the US Financial Advisor in fact strongly opposed the creation of this kind of dual currency system and had pressed the government very vigorously not to make the dollar legal tender. The government, however, insisted on this provision because of "its distrust of the National Bank and the latter's owners, the National City Bank of New York, which it did not wish to see as the sole source of currency issues in Haiti" (Moore 1972: 268 fn.45; see also pp.56-7). Moore does not explain the basis of the US position, but it may have been influenced by the interests of the National City Bank itself whose seigniorage profits would have been bolstered if it had become the monopoly issuer of currency.[6]

The interest within US financial circles in promoting the dollar's use in Latin America reached a highpoint in 1915 when Kemmerer put forward a proposal for

creating "Pan-American monetary unity" at the Second Pan-American Scientific Conference. The kind of monetary union he was proposing was not the kind we think of today where national currencies are replaced by a single supranational currency. Instead, he had in mind the example of the Latin Monetary Union and Scandinavian Monetary Union that had existed in Europe since 1865 and 1873 respectively. These unions created a common monetary unit and then allowed each other's currencies to circulate freely in their respective territories. In Kemmerer's proposal, all countries in the Americas (including Canada) would adopt a common monetary unit that was equivalent to the US gold dollar (he suggested that it might be called the "oro"). At the time of his writing, the only countries that had already done so were Panama, Cuba, the Dominican Republic, Nicaragua and Canada; other Latin American countries had units assimilated to either the British pound or the French franc (Kemmerer 1916b: 73fn3).[7] Each country would then allow other members' gold coins to be used within their territory; indeed, he suggested that each country's gold coins might bear the words "Pan-American Union" along with their value in "oro" to facilitate their widespread circulation. In practice, this proposal would have encouraged the wide use of US currency across the Americas because of the confidence the dollar commanded vis-à-vis locally issued currency.

The link between monetary unity and the idea of Pan-Americanism had in fact first been made a quarter century earlier at the First Pan American Conference in 1889-90. At that conference, the US had asked delegates to consider the adoption of a common silver coin as a way of fostering regional commerce, an idea that met with some support among Latin American delegates (Inman 1965: 41; Smith 2000: 22-3).[8] Kemmerer made the same case; a common gold coin and gold-based monetary unit equivalent to the dollar would dramatically reduce international transaction costs associated with intra-regional trade and investment. This would not only benefit businesses and travellers but also help to encourage US investment to flow to poorer regions of the Americas. He also argued that it would have a higher ideological value: "The existence of a unified monetary standard, with gold coins bearing the emblems of Pan-Americanism circulating throughout the two continents would be a perpetual symbol of the Pan-American ideal" (Kemmerer 1916b: 71).

The Director-General of the Pan-American Union, L.S.Rowe, quickly endorsed Kemmerer's idea and "had Kemmerer's speech printed and distributed widely in Latin America" (Rosenberg 1999: 102). The idea also met with some support in Latin America. At the same 1915 conference, other proposals for a Pan-American monetary union were put forward by delegates from Chile and Nicaragua (Seidel 1973: 92fn33). But at the time, the US enthusiasm for economic dimensions of Pan-Americanism also frequently met with skepticism from many in Latin America who them as a cover for the extension of US economic interests in the region (Sheinin 2000).

From Dollarization Diplomacy to De-Dollarization Diplomacy

Kemmerer's ambitious proposal was never implemented. US policymakers not only abandoned the idea of promoting a common monetary standard during the 1920s. By the 1940s and 1950s, they were actively encouraging many countries in the Caribbean and Central America to "de-dollarize" their domestic monetary systems. In several short decades, US policy had done a complete about face. What explains this change?

The abandonment of Kemmerer's Pan-American monetary vision during the 1920s was on the surface puzzling. After all, Kemmerer acquired enormous political influence throughout Latin America as an advisor to governments considering monetary reforms during the 1920s (e.g. Drake 1989). Interestingly, however, he turned his back on his own idea as early as 1921 (Rosenberg 1999: 287fn26).[9] In the face of rising Latin American nationalism and growing US domestic opposition to dollar diplomacy during the 1920s, he seemed to recognise that his earlier proposal was now too ambitious. As he put it, US officials had to acknowledge that the maintenance of nationally-distinct monetary units was "a natural reasonable function of a sovereign state" (quoted in Rosenberg 1999: 103).[10]

The economic and political upheavals of the early 1930s ensured that the idea of a monetary union across the Americas lost whatever support it might have still had within US policymaking circles. With the onset of the Great Depression, the export markets of Latin American countries collapsed as did US foreign lending to the region. Faced with severe balance of payments crises, most Latin American government chose not to undergo dramatic deflations, but rather to suspend payments on foreign debts, introduce trade and exchange controls, and/or devalue their currencies. These economic changes were accompanied by political ones as the liberal oligarchic regimes of the 1920s soon gave way in many countries to more nationalist governments that experimented with more activist monetary policies aimed at financing government spending and producing domestic economic growth. In this context, the idea of a regional monetary union centered on gold-based currencies made little political sense any more. Even if it had, US policymakers no longer showed much interest in this kind of economic internationalism. With the election of Roosevelt, the financial elite that had favored "gold standard diplomacy" lost political influence and even the US itself soon left the gold standard. The new Roosevelt administration further signalled its desire to distance itself from past US foreign policy towards Latin America within its "Good Neighbour" policy that renounced US military intervention in the region.

These dramatic economic and political developments did not, however, prevent the continued use of the dollar in places where it was already firmly entrenched such as Cuba, Panama, Honduras, Haiti, Puerto Rico and the Dominican Republic. While most Latin American governments devalued their currencies against the dollar, none of these dollarized regions did. [11] The dollar's widespread use in fact ensured that export elites and foreign companies had less incentive than elsewhere to press for a devaluation (e.g. Bulmer-Thomas 1987). But the issue of the dollar's role did still increasingly became a flashpoint for nationalists in the region. In Panama, for example, the nationalist President Arnulfo Arias who came to power in 1940 sought to reduce the dollar's role in the country as part of his broader challenge to the influence of the US (and local oligarchs). He ordered paper balboa notes to be issued for the first time in the country's history and hoped the break the link between the balboa and the dollar. When his government was overthrown only seven days after issuing the notes, however, this money was quickly withdrawn (LaFeber 1989: 73-77, Grigore 1972).

The role of the dollar also became a controversial issue in Cuba during the dramatic political upheavals of 1933-4 in that country. In late 1933, a nationalist government came to power without US support that was dedicated to the protection of national sovereignty as well as various economic, political and social reforms (e.g. Perez 1986). As part of these objectives, it challenged the dominance of the dollar by

announcing plans to expand the issue of Cuban silver coins dramatically as well as increase the portion of taxes that could be paid in them from 20 to 70%. Its primary goal seemed to be to capture seigniorage profits that were lost to the US through the dollar's circulation, an issue that had attracted the attention of Cuban nationalists during the 1920s (Wallich 1950: 48, 84-5). The government that followed it in 1934, while more conservative in most respects, pursued this policy further when it made Cuban currency unlimited legal tender not just for tax payments but for all private payments. These moves, which were accompanied by the introduction of exchange controls, were designed to create a whole new monetary system that was independent of the US dollar. Again, the government's motivation was primarily to expand its own financial resources; it hoped to print money to finance emergency loans designed to stave off the financial collapse of many domestic businesses. When these monetary reforms produced massive capital flight and strong opposition from banks, however, the government abandoned its ambitious goals of eliminating the dollar's use (Wallich 1950: 86-7, 112; Diaz-Alejandro 1988: 196). But further issues of silver coins as well as new notes (decorated with images of Cuban nationalist heros[12]) throughout the rest of the decade dramatically reduced the dollar's role within the Cuban monetary system .

Since these moves were often seen to challenge US influence, it may seem surprising that the US itself began to endorse "de-dollarization" in many of these countries during the 1940s. In 1942, a US Technical Mission to Cuba recommended the establishment of a central bank and the complete withdrawal of dollars from the monetary system (Triffin 1944).[13] In a 1947 mission to the Dominican Republic, representatives from the US Federal Reserve advised the local government to eliminate the dollar's use and issue a new national currency, advice that was quickly followed. An IMF mission including a key Federal Reserve official to Honduras in 1950 recommended that the US dollar no longer be used in the domestic economy, a move that was soon carried out. Indeed, this official trumpeted the fact that “[f]or the first time in its history, Honduras will then have nationalized its currency” (Vinelli 1950: 428).[14]

What explains this new "de-dollarization diplomacy" of the US? Within existing scholarly literature, US foreign monetary policy towards Latin America during the 1940s and 1950s has received very little attention. This is surprising given the important role it played in transforming the domestic monetary systems of the countries above as well as many others during this period. The neglect of the subject is particularly unfortunate given the interesting content of their advice. Led by Robert Triffin of the Federal Reserve, US "money doctors" in this period explicitly turned their back on the ideas of Conant, Jenks and Kemmerer. This was true not just with respect to dollarization but on a whole range of other monetary issues. The new money doctors were willing to endorse the use of capital controls, activist monetary policy, and adjustable exchange rates. Each of these policies would have been an anathema to the earlier monetary doctors. a point that Triffin and his Federal Reserve colleagues were very happy to acknowledge (Helleiner forthcoming)

Their decision to reject earlier US monetary advice was not taken lightly. In response to a request for monetary advice from Paraguay in 1941, Triffin - in his role as chief of the Latin American section of the staff of the Federal Reserve's Board of Governors - had launched a detailed process of consulation with financial officials from the US and other Latin American countries over a several year period. Out of this process, he and other key Federal Reserve officials concluded that a different approach to money doctoring

would be necessary. This new approach was first put into place in Paraguay in a set of monetary reforms in 1943-45 which Triffin (1946:25) himself described as "revolutionary". The Paraguayan model of reform was then promoted actively by Triffin and other US officials in a series of "money doctoring" missions over the following decade not just in the countries mentioned above but also Guatemala (1945), the Philippines (1949), South Korea (1950), and Ceylon (1950) (Helleiner forthcoming).

Various publications by Federal Reserve officials in this period outline clearly their rationale for the new approach to money doctoring (Federal Reserve 1945, Triffin 1944, 1946, 1947a,b). They argued that the interwar experience had highlighted the drawbacks of the gold standard and a passive monetary policy geared externally to respond automatically to changes in the balance of payments. In countries whose balance of payments were vulnerable to crop failures, dramatic changes in export markets, or volatile international capital movements, this "monetary automatism" was simply too costly in an economic and social sense. It magnified – rather than minimized - the impact of international instability on the domestic economy. In the new American view, what was needed was a form of monetary management that *insulated* the national economy from international disruptions rather than *reinforced* the latter's impact on the former. Whereas Kemmerer and his colleagues had prioritized the external stability of the currency and international equilibrium, the new priority was domestic economic development. From this goal stemmed their endorsement of activist monetary policies, adjustable exchange rates, capital controls, and especially the removal of foreign currencies from the domestic monetary system.

The latter was, in fact, a key precondition for the other policies to be implemented effectively. It was very difficult, US officials argued, for a central bank to pursue an independent monetary policy devoted to national development unless the national currency held a monopoly position inside the country. In the Dominican Republic, for example, Wallich and Triffin (1953: 26) noted that "the continued existence of dollar contracts and payments would deprive the monetary authorities of much of their power". In Cuba, Wallich (1950: 154-6) also noted that dollarization prevented the country's foreign exchange resources from being under the kind of centralized control that would have enabled monetary authorities to mobilize them efficiently to promote development goals. He also highlighted how capital controls were much more easily evaded in countries where dollars were in widespread use (Wallich 1950: 89-92).

These various arguments were in effect an indictment of earlier US policy. One US official involved in the 1950 Honduran reforms, for example, lamented how the monetary system had "not been used an as instrument to promote economic development" in the past, but that now it would be able "to assist the growth of the national economy" (Vinelli 1950: 420). In the Cuban context, Wallich (1950: 43) noted that an independent currency in the 1930s would have enabled Cuba to avoid the "very painful" adjustments it had undergone during the depression and he evaluated the 1934 Cuban initiative to eliminate the dollar very sympathetically (Wallich 1950: 86-92, 112, 216). US officials also sometimes highlighted that the use of the dollar had meant that countries were "in effect making a loan to the United States" (Wallich 1953: 45; see also Wallich and Triffin 1953: 24). More generally, they also highlighted the broader political significance of the removal of dollars from the domestic monetary system. Here, for example, is how a US official explained the advantage of de-dollarization in Honduras:

"In international affairs, it will strengthen the position of the Republic and put it on an equal monetary footing with all other nations" (quotation from Vinelli 1950: 428).

If these were the rationales US officials gave for turning their backs on past US policy, we still need to explain the political factors that encouraged this shift in priorities. Part of the explanation relates to an ideological transformation that took place in the wake of the New Deal and the Keynesian revolution. As John Ruggie (1983) has described, US foreign monetary policymaking in this period was heavily influenced by the emergence of an ideology of "embedded liberalism". Those influenced by this ideology sought to find a way to reconcile the new domestically-oriented welfarist goals of the New Deal and Keynesianism with the rebuilding of an open multilateral world economy. In the monetary sphere, this led them to reject the gold standard in favor of an international monetary system that endorsed capital controls, adjustable exchange rates, and the provision of balance of payments financing. Although Ruggie focuses on how this vision influenced the Bretton Woods conference in 1944, it also clearly influenced the kind of advice Triffin and other economists in the US Federal Reserve gave to Latin American countries (Helleiner forthcoming).

Even if US officials were not themselves convinced by this new thinking, they were forced to recognize that Latin American governments had little interest in returning to the gold standard and the classical liberal approaches to monetary policy of the pre-1930s period. Triffin (1944), and other US officials were very knowledgeable about policy trends in Latin America during the 1930s and they understood the extent to which new approaches to monetary policymaking had become politically entrenched in the region. Challenging these new approaches might not just be futile but also detrimental to broader US geo-strategic goals. In the 1938-1941 period, US foreign economic policy towards Latin America underwent a dramatic change in response to fears about the growing links between Latin American nationalists and the Axis powers. To counter Axis influence, Gardner (1964: chs.6,10) explains how US officials decided to take a more active and positive role in supporting Latin American nationalist goals of economic development and industrialization. The new US monetary advice to Latin America fit this pattern perfectly. The initial US monetary consultations with Paraguay took place at a time when US policymakers were actively seeking to prevent its government from allying itself too closely with the Axis powers. Triffin also went out of his way to consult with Raul Prebisch in developing the initial Paraguay reforms. Prebisch, who was head of the Argentine central bank between 1935-43 and then became head of the UN Economic Commission for Latin America, was the leading theorist of the "structuralist" school that advocated economic nationalist policies of import-substitution industrialization.[15]

After the initial concern about Axis influence diminished, the US had other strategic reasons to continue to support this approach to money-doctoring during the 1940s and 1950s. With the onset of the Cold War, US policymakers recognized that their accommodating approach towards economic nationalism in the monetary sector could help cultivate allies abroad. The promotion of strong domestic economic growth in Southern countries - as opposed to monetary orthodoxy - was also seen as a tool to undermine the political strength of left-wing opposition in those countries. I have also shown elsewhere how the US approach to money doctoring enabled the US to gain influence in ex-British colonies, such as Ceylon and Ethiopia. Its more sympathetic

approach to these countries' nationalist monetary goals contrasted sharply with the orthodox advice given by British officials at the time (Helleiner forthcoming).

What of the role of US business preferences? During the 1900-15 period, US business interests, especially those in the financial sector, often strongly supported US monetary advice to Latin American countries. One would expect, then, that there was US business opposition to the new "money doctoring" approach. In fact, however, as Maxfield and Nolt (1990) have noted, key US business interests were supportive of the US decision during the 1940s and 1950s to support import-substitution industrialization in Latin America and elsewhere. To be sure, ISI policies were not generally favored by smaller US exporters of finished goods or US investors in Latin American export-oriented mining and agricultural sectors. But these policies did find support among large US manufacturing interests that were interested in both exporting capital goods and heavy machinery to the region and establishing branch-plants behind Latin American tariff walls (Maxfield and Nolt 1990: 50; Gardner 1964). It was this latter "bloc" - rather than the financial interests who had been powerful in the pre-1930s period - that provided the dominant business influence on US foreign economic policymaking during this period.

The Revival of Interest in Dollarization Diplomacy Today

Given the way that US money doctors discredited the idea of dollarization in Latin America during the 1940s and 1950s, it is interesting to see this issue reemerge on the US agenda today. This development is particularly intriguing because US policymakers are debating an even more ambitious idea than the kind of partial dollarization that was promoted in the early 20th century (outside of Puerto Rico). Now, proponents are encouraging Latin American countries to dollarize fully; that is, to abandon their national currencies and adopt the US dollar as their exclusive currency.[16] If the goal is more ambitious, the means of reaching it are less so. They propose that the US offer encouragement in a more subtle way than the gunboats that were often used in the past: the US could simply offer to compensate Latin American governments financially for the most (85%) of the lost seigniorage they incurred from adopting the dollar. In 1999, a bill was submitted to both the US Senate and House of Representatives that would empower the Treasury Secretary to act in this way and hearings on this "International Monetary Stability Act" were held.

What explains this turn of events? The history analyzed in this paper is useful in helping us to answer this question. To begin with, it highlights the key role of prevalent macroeconomic ideologies in influencing US views towards dollarization. The rejection of dollarization by US money doctors in the 1940s and 1950s stemmed primarily from their "embedded liberal" ideology that advocated activist monetary policy as a tool to promote growth and employment. But for the US advisors earlier in the century, the proper goal of monetary policy was much more limited: to provide price stability. From this "classical liberal" perspective, there was nothing wrong with dollarization. Indeed, it could help discipline local policymakers who might have more ambitious and interventionist ideas about monetary management. Given this history, we should not be surprised to learn that the renewed interest in promoting dollarization in Latin American is strongest among those who reject monetary activism in favor of a "neoliberal"

approach that identifies price stability once again to be the primary goal of monetary policy.

The Republican Florida Senator (now retired) who initially played the leading role in sponsoring the dollarization bill in US Congress - Connie Mack - provides a good example of this point. He has long been an advocate of this neoliberal view; indeed, he has proposed legislation that would make price stability the principal goal of the Federal Reserve System. He explains his interest in dollarization abroad as an extension of the monetary principles he has promoted at home: "Those of you who know me know that it's a long-standing aim of mine that the United States ought to seek not only to export our products but to export our principles as well….in terms of global growth, our #1 export right now ought to be our principled approach to price stability" (Mack 2000: 2). Like Mack, several people who testified before Senate committees in favor of the bill also linked the promotion of the dollar abroad to the domestic goal of making price stability the primary aim of US monetary policy. If the latter reform was undertaken, they argued, Latin American countries might be more inclined to adopt the dollar as their currency.[17]

The new US interest in promoting dollarization is thus partially linked to a disillusionment with the kinds of activist national monetary policies that became popular during and after the 1930s. The experience of stagflation during the 1970s played a key role in prompting this change in macroeconomic thinking. Stagflation was explained at the time by many critics of Keynesianism as a product of inflationary expectations that grew out of activist monetary policies. This analysis played an important role in convincing many policymakers to embrace a "neoliberal" view that monetary policy has no long-term impact on real output and employment, and that the maintenance of price stability should once again be the primary objective of monetary policy. The growing power of global financial markets also reinforced the argument that monetary authorities should re-establish their credibility and reputation for producing stable money by a strong commitment to price stability (Andrews and Willett 1997; Maxfield 1997).

Neoliberal advocates of dollarization make arguments that are quite similar to those made by Conant, Jencks, Kemmerer in their defense of the gold standard in the early 20th century. By providing greater domestic price stability, dollarization will, they argue, encourage domestic savings, the development of deeper financial markets, and a more stable macroeconomic environment for capital accumulation. It will also discipline policymakers from over-spending by eliminating the possibility of printing money. In addition, by eliminating the exchange rate risk vis-à-vis the dollar, dollarization will foster foreign investment and trade as well as remove the need for exchange controls. They also reject the post-1945 view that exchange rate movements can play a helpful role in fostering macroeconomic adjustments, or in providing a degree of macroeconomic autonomy. Given the volatility of exchange rates today, they argue that exchange rates are not able to perform that kind of useful adjustment function or provide autonomy for a country to pursue an independent monetary policy. Interestingly, in developing these arguments, the case of Panama is now often used as a positive example for other Latin American countries to emulate.[18]

It is also important to note that the new interest of US neoliberals in dollarization abroad emerged from the context of the dramatic currency crises of 1997-98. During these crises, many US neoliberal thinkers and politicians were very critical of the large loans that the IMF extended to crisis-stricken countries and the heavy conditionality

associated with these loans. Many of these critics began to look at dollarization as alternative way of promoting monetary stability abroad that would no longer require this kind of foreign financial support. As Mack (2000: 3) put it, "I see dollarization as an antipoverty, prodevelopment policy….By eliminating the root cause of currency crises, widespread dollarization would eliminate the need for international institutions to make the complex and highly controversial interventions in national economies that have been an integral part of recent currency rescue efforts."

In addition to the role of ideology, we have also seen that US policy towards dollarization in the past has been influenced by economic interests. Again, there are parallels between the early 20th century period and today. Once again, US advocates of dollarization today argue that the elimination of an exchange rate risk will foster US trade and investment with Latin American countries (Schuler and Stein 2000: 5). In an era when the US is actively cultivating these links through its efforts to build a Free Trade Area of the Americas, this point carries considerable weight. As one supporter put it, "'I suspect that simply switching to a common currency would promote hemispheric integration as effectively as would many thousands of man-hours devoted to the ongoing negotiations over a free trade agreement for the Americas".[19]

The way that dollarization might provide US businesses with an advantage vis-à-vis foreign businesses in Latin American markets has also been raised by US policymakers. As then Deputy Treasury Secretary Larry Summers (1999: 3) put it in his Congressional testimony, "to the extent that dollarization helped to consolidate or expand our large role in Latin American markets, it might help to ensure that we continued to benefit disproportionately from the future growth". The 1999 Economic Report of the President highlighted that US financial institutions might stand to gain particularly from dollarization (Bogetic 2000: 6). It is clear, for example, that dollarized countries would be strongly encouraged by the US to open up their financial sector to US financial institutions as a way of fostering a stable banking system. Indeed, the International Monetary Stability Act lists this as one of various criteria that the US Treasury Secretary is supposed to considering in determining whether a country should be "certified" to receive seigniorage revenue (Schuler and Stein 2000: 8). Once they are in Latin American dollarizing banking systems, both Cohen (forthcoming) and D'Arista (2000;5) also note that US banks will have a competitive advantage because they have privileged access to the Federal Reserve's resources. This prediction is supported by the experience of the 1920-21 Cuban financial crisis which left US banks in a dominant position after their Cuban counterparts collapsed without access to foreign emergency funds.

In the past, US policy towards dollarization was also influenced by broader political and strategic concerns. We have seen how some US policymakers in the early 20th century saw the use of the dollar abroad as important symbol of US authority abroad. In the current era, the 1999 Economic Report of the President noted in a similar fashion that dollarization could contribute to the "power and prestige" of the US by boosting the dollar's role as an international currency (quoted in Bogetic 2000: 6). More specifically, dollarization diplomacy in that earlier era was also linked to a broader rivalry with European powers. This issue has also resurfaced today in the context of the creation of the euro by European Union countries and concerns that the world is dividing into giant monetary blocs. During the hearings on dollarization, one Senator, Jim Bunning, expressed the following concern: "Are they using the Euro to try and grab a greater share of

the expanding Latin American markets and cut into US exports in our Hemisphere?" (US Senate 1999a). A broader point was made by influential Congressional staff members: "[Dollarization] would help the dollar remain the premier international currency, a status that the euro is now challenging. Dollarization by one or more large Latin American countries would significantly expand the number of people officially using the dollar, moving the population of the dollar zone ahead of the population of the euro zone for the time being" (Schuler and Stein 2000: 7).

Cohen (forthcoming) has also noted that dollarization could give the US extra leverage over Latin American governments. He recalls the way in which Panamian government was vulnerable to US monetary pressures during the Noriega years because of its dependence on the dollar for its currency (see also Kirschner 1995). The process of sharing seigniorage with dollarized Latin American countries could also be used as a tool of US influence. The International Monetary Stability Act would have given the Treasury Secretary enormous discretion to decide whether or not to share seigniorage with a particular government. In the words of two Congressional staff members: "even if a country does fulfill all of the considerations, the Secretary can still deny it a rebate. The latitude that the Secretary has is one factor that should induce countries to interested in official dollarization to cooperate fully with the United States" (Schuler and Stein 2000: 9).

There are, thus, some interesting parallels between the basis of support for dollarization diplomacy in the early 20th century and that today (although these parallels should not of course be overstated). Does this mean that the US is about to come full circle, turning its back on the intervening years when dollarization diplomacy was rejected? This is far from clear. Senior officials in the Clinton administration were unwilling to endorse Mack's initiative during Congressional testimony and the bill did not progress pass the committee stage. Despite the support that exists in some quarters, it is apparent that US policymakers are more reticent about the idea of endorsing dollarization diplomacy than they were a century ago.

Perhaps not surprisingly, their reasons parallel some of those that prompted US officials to reject dollarization diplomacy after World War One. While US policymakers no longer endorse the kind of ambitious Keynesian policies of the mid-century, many still remain committed to the idea that exchange rate flexibility and discretionary domestic monetary policy have an important role to play in Latin American countries (e.g. Summers 1999: 2). US officials also are wary of stirring up Latin American nationalist sentiments. Given the history of the early 20th century, it is easy for critics to portray dollarization diplomacy as "reinventing colonialism" (D'Arista 2000:3). If countries did decide to dollarize, US policymakers also worry that "in difficult times, the loss of domestic monetary sovereignty would foster resentment and encourage policy makers to deflect blame for problems onto the United States" (Summers 1999:3). Even strong supporters of dollarization go out of their way to accommodate nationalist sentiments abroad by highlighting that the International Monetary Stability Act does not pressure any Latin American country to dollarize. As Mack (2000: 3) acknowledges, the decision to dollarize "touches on a nation's very sense of self: the way in which maintaining a separate currency underscores a nation's sovereignty….It's a concern to which we must be sensitive. The plan I've set out is all carrot and no stick." (see also Schuler and Stein 2000: 7)

Supporters are indeed quick to point out that the issue is being discussed in the US only because it was first raised by Argentine officials when they were considering full

dollarization in early 1999. At that time, these officials approached the US government to ask what kind of support the US might be willing to provide if their country was to adopt the dollar as Argentina's sole currency. Argentina had already partially dollarized in the early 1990s in the wake of a hyperinflationary experience and it now was considering full dollarization in order to eliminate currency-related risk premium that foreign investors still assigned to the country's borrowers. Argentina's interest in dollarization is not an isolated case: both Ecuador and El Salvador each chose to abolish their national currencies and adopt the US dollar in 2000 and 2001 respectively and this move is also being debated prominently in countries such as Costa Rica, Guatemala and Mexico.

These developments are a sign of the extent to which views in some parts of Latin America had changed since the middle decades of the 20th century. The new Latin American interest in dollarization is a product partly of the ascendancy of neoliberal monetary ideas in these countries and partly of the acute desire of these countries to attract foreign investment (Jameson 2001b). Whatever its cause, this interest has certainly made it easier for US officials to deflect criticism that dollarization is a US-led initiative. But Latin American support for dollarization also should not be overstated. Nationalist opposition has been quite present in many of the cases just mentioned and US officials are no doubt correct in their assessment that it could easily grow if the US was seen to be promoting dollarization very strongly.

The specifics of the Argentine request highlight that US policymakers may also be constrained by domestic isolationist sentiments within the US from promoting dollarization abroad more actively. According to some reports, Argentina's government indicated in 1999 that it would be more willing to consider adopting the US dollar if the Federal Reserve would agree to assume some lender-of-last-resort functions for Argentine financial system (Cohen forthcoming). This request recalls earlier US practice; as noted above, the US Federal Reserve established agencies in Cuba to provide lender-of-last-resort facilitities for institutions operating in that dollarized monetary system. In the current era, however, there is little support for this kind of economic internationalism within the US today. Mack's Act specifies clearly that the Federal Reserve is not obligated to serve as a lender of last resort to any dollarized country and US officials have bent over backwards to stress to Congress that the US would not even consider this kind of role. (Summers 1999; see also Schuler and Stein 2000).

Finally, what about the role of business preferences? As we have seen, de-dollarization diplomacy in the 1940s and 1950s found support among certain segments of the business community that saw their economic interests increasingly tied to more inward-looking, growth-oriented economic policies in Latin America in the 1940s and 1950s. That bloc of US business support for ISI policies in Latin America no longer exists as a prominent political force in US politics. Does that then leave the field open for other parts of the US business community - most notably the internationally-oriented financial sector - to push for dollarization? It is certainly true that some Wall Street interests testified in favor of dollarization at Congressional hearings (although one opposed it).[20] But the significance of this point should not be exaggerated. As Cohen (forthcoming) notes, the debate on dollarization does not yet appear to have generated much interest at all from the US business community. Although supporters of the Mack bill argued that businesses will benefit from lower transaction costs, US businesses themselves does not appear so concerned about the issue.[21]

Conclusion

The pros and cons of dollarization diplomacy in Latin American have not been debated in the US for many decades. For this reason, the current debate may have appeared to be an entirely new one for the current generation of US policymakers. As I have shown in this paper, however, there are two previous moments in US history when the issue has been a prominent one. Between 1900-1915, the US devoted considerable attention to the task of promoting the use of dollar within many Caribbean and Central American countries. Then, in the 1940s and 1950s, US policymakers set out to undo the work of their predecessors.

Recalling these earlier episodes not only provides an interesting perspective on current debates. I have tried to show in this paper how it also can help us understand the politics that influence US monetary policymaking in this area. US support for dollarization abroad, after all, has some of the same roots today that it had in first two decades of the 20th century. In both eras, those interested in fostering US economic interactions with Latin America have seen dollarization as a way to eliminate currency-related transaction costs altogether. Advocates of the liberal monetary goal of price stability have also been leading proponents of dollarization diplomacy then and now. The monetary project has also been linked in both eras with the extension of US power and influence abroad.

At the same time, many US policymakers remain very wary of dollarization diplomacy for similar reasons as those that emerged in the middle decades of the century. In each era, opposition to the practice has come from those who believe that discretionary management of a national exchange rate and/or domestic money supply is a key tool for development. US officials have also been wary in both eras of offending Latin American nationalist sentiments as well as those with more isolationist leanings at home.

The current debate within the US about dollarization diplomacy is thus strangely reminiscent of some aspects of both of these two previous episodes. This makes it particularly difficult to predict whether US policy is likely to come full circle back to the kind of dollarization diplomacy it practised a century ago. But this historical perspective does at least help us to identify some of the kinds of political variables that are likely to influence US international monetary policymaking in this area in the future.

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[1] The only scholar to devote some attention to this historical context that I have found is Kenneth Jameson (2001a, 2002).

[2] In the Cuban context, for example, Wallich (1950: 42) noted that the business community "speak of the dollar circulation in Cuba as a great confidence-creating element." Interestingly, in the Haitian case as I note below, the local government saw the circulation of dollars as a way to discipline the behavior of the US-controlled bank that issuing the local currency.

[3]This decision was also influenced by the US fear that they would have difficulties preventing counterfeiting of US dollars in a context where "a strong secret service had not yet been extended throughout the country" (Kemmerer 1916a: 305)

[4] It is also worth noting that the US dollar became increasingly used in many other Latin American countries during this period without direct US influence being involved. In Mexico, for example, dollars were used extensively during that country's revolution when trust in domestically-issued currency collapsed.

[5] Honduras did finally introduce a new national currency on gold exchange standard in 1931 and then it followed the US off gold soon after.

[6]The National City Bank was heavily involved in influencing US policy towards Haiti in this period and its seigniorage profits were an issue at the time (e.g. Douglas 1994: 38-9; Plummer 1992: 96-8).

[7] He noted, however, that many other Latin American countries did allow US gold coins to circulate legally within the domestic monetary system such as Columbia, Costa Rica, Ecuador, El Salvador., Haiti, Paraguay, Uruguay, Venezuela.

[8] The issue had also come up subsequent meetings, such as at the Third Pan American Conference in 1906 (Rosenberg 1999: 23). It had also arisen at the Pan-American Financial Conference earlier in 1915 (Gilderhus 1986: 61). Kemmerer (1916: 74fn2) noted that a similar proposal for "monetary unity" within central America based on a gold unit equivalent to the US dollar had promoted by Honduras and discussed at conferences in 1909 and 1910. He now sought to expand the idea to the whole of the Americas.

[9] Some countries that Kemmerer advised during the 1920s, however, did introduce new currencies whose gold content was identical to that of the US dollar. See for example Guatemala's reform (Kemmerer and Dalguaard 1983: 36).

[10] Kemmerer may also have influenced by the views of prominent liberal financial policymakers elsewhere in the world at this time. In Europe, in particular, there was a broad disillusionment within liberal circles with the idea of currency unions in the early post-1918 world. In part, this reflected a recognition that such unions were no longer compatible with the heightened nationalist sentiments of the age. But it also stemmed from the experiences of the LMU and SMU which had encountered enormous difficulties when member currencies had been inconvertible during and after the war. These difficulties produced considerable political tensions that eventually led to the unravelling and dissolution of the unions in the early-to-mid 1920s. These unpleasant experiences encouraged liberal policymakers at the influential Brussels international monetary conference in 1920 to reject proposals for the creation of international currencies or common units of account. Other proposals for monetary unions in Europe in the early 1920s was also consistently rejected by powerful policymakers on the League of Nations Financial Committee (Helleiner forthcoming).

[11] Some of these countries did, however, stop payments on debts and introduce exchange controls.

[12] These figures included people as Jose Marti, Maximo Gomez, and Carlos Manuel de Cespedes (Museo Numsmatico 1980: 47-55).

[13] The central bank was established in 1948, but I have not yet been able to determine when a de-dollarization initiatives was undertaken by the Cuban government. In his 1950 book, Wallich (1950: 32, 218) suggests that the dollar's elimination from Cuba was about to take place.

[14] Both Panama and Puerto Rico retained the dollar throughout this period and still do today. I have not yet been unable to determine the pattern of Haitian policy towards de-dollarization during these years.

[15] The head of the Bank of Colombia (Enrique Davila) was also very involved in Paraguayan consultations with Triffin and both he and Prebisch even spent 3 months in Paraguay in 1943 and 1945. Other Latin American governments, such as that in the Dominican Republic, also invited Prebisch for consultations with US officials as part of the preparations for US-led monetary reform programs (Wallich and Triffin 1953: 25).

[16] Some advocates suggest that countries could continue to produce their own subsidiary coins.

[17] See for example the testimony of Judy Shelton and Wayne Angell in US Senate (1999a).

[18] For these various arguments in favor of dollarization, see for example Schuler and Stein (2000), Schuler (2000), Hausmann (1999).

[19] Michael Gavin of Warburg Dillon Read in US Senate (1999b). Congressional staff advisors to Mack have also argued that dollarization would benefit US-based business by eliminating the prospect of competitive devaluations in Latin American countries (Schuler and Stein 2000: 7). Gavin (in US Senate 1999b) suggests that US labor would benefit for the same reason, but D'Arista (2000) disputes this view on the grounds that dollarization abroad would encourage an export of capital from the US and encourage Latin American economies to become even more export-oriented.

[20] For the supporters, see the testimony of David Malpass (of Bear, Stearns and Co.) and Michael Gavin (of Warburg Dillon Read) in US Senate (1999b). The opponent was Walter Molano (of BCP Securities) who made an interesting argument that the existence of a national currency ensured that external creditors were often repaid in a priority fashion during debt crises because governments essentially imposed an inflation tax on the local population. He concluded: "Unfortunately, dollarization bumps local currency holders up the seniority ladder and allows them to be paid prior to the external creditors" (Molano 2000: 5)

[21] In a similar way, McNamara (1998: 37-41) notes that there is also not a great deal of evidence that European business has been a major promoter of EMU because of concerns about international transaction costs, even though they are dealing with a very large number of national currencies.