The original documents are located in Box B65, folder "International Monetary Crisis, 1971 (2)" of the Arthur F. Burns Papers at the Gerald R. Ford Presidential Library.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date May 6, 1971

To Chairman Burns

Subject: 2:45-3:00 Market Report

From Paul Kelty

Domestic Securities Markets

Prices of U. S. Government securities are somewhat higher now than at their opening levels today, although the market is still very uncertain. Most issues are now about 2/32 higher to 2/32 lower on the day. The two when-issue notes are slightly higher than their 11:00 o'clock levels. The 5's of 8/72 are quoted 99.31--100.02, while the reopened 5-3/4's are at 99.18--.22. Selling pressures in the when-issued notes have abated relative to yesterday, although investor demand for them is said to be light. Treasury trust accounts have purchased some $35 million of coupon issues today.

The tone in the bill market is firm, with most issues now about 1 to 9 basis points lower on the day. The 3-month bill is down 9 basis points to 3.83 per cent bid. Dealers have reported a good demand for bills today, including a large amount of buying by Japan. The dealers also anticipate a good reinvestment demand to stem from the outflow of dollars abroad. Moreover, the market is in a good technical position.

Federal funds are trading at 4-5/8 and 4-3/4 per cent, with the quote ranging between 4-1/2 and 4-3/4 per cent. The System has made $949 million of repurchase agreements, including $882 million against Governments and $67 million on bankers' acceptances.

The corporate and municipal bond markets are quiet with relatively little price change. In the stock market, the Dow-Jones industrial average was up 1.90 points at 2:00 P.M.

CONFIDENTIAL (FR)

May 6, 1971

To: Chairman Burns

From: Jan W. Karcz

Subject: Foreign Exchange Market - 2:30 Call.

With most European central banks not supporting the dollar, exchange markets were much quieter today. Euro-dollar rates firmed very sharply as a scramble for dollars needed to cover last two days' sales developed; the overnight rate at one point reached 40 per cent.

Most rates varied erratically in response to various statements by West German officials but on balance changed little from yesterday's close. At 2:15 the premiums on the official ceiling rates were:

Deutsche Mark	+ 1.49
Swiss Franc	+ 3.50
Guilder	+ 1.04

The only central bank intervention reported was by the Bank of Japan which took in $330 million; the bank issued a statement that the present yen parity will be maintained.

At 11:00 the covered arbitrage calculations were:

U.K. local authority	6.48	Canadian bills	2.95	Canadian fin. paper	3.88
3-mo. Euro-$	7.63	U.S. bills	3.86	U.S. fin. paper	4.50
Gross advantage	1.15	Gross advantage	0.91	Gross advantage	0.62
Sterling discount	0.82	C$ premium	1.33	C$ premium	1.33
Net, favor Euro-$	2.97	Net, favor Canada	0.42	Net, favor Canada	0.71

DRAFT-2:PAV:5/6/71

After full review of the recent developments in international financial markets, Secretary of the Treasury John B. Connally today again expressed the view of the United States Government that existing exchange rate parities would provide an appropriate basis for the re-opening of exchange markets in various European centers. Such action in the interest of international monetary stability will require further close cooperation among national monetary authorities, particularly in dealing with the problems posed by large, short-term capital movements. As in the past, the United States is prepared to participate fully in such immediate cooperative action.

The current disturbances in the exchange markets also heavily underscore the urgency of dealing with the outstanding problems of the international economic system. Certain of these problems, growing out of the enlargement of the Eurodollar market and the volatility of short-term capital flows, have already been the subject of review by central banking and government officials. We expect that review to be intensified, with conclusions reached promptly.

The underlying deficit in the balance of payments -- estimated at some \$2-1/2 - \$ 3 billion -- must be dealt with in a forcible manner. Totthat end, the United States has undertaken a full review of relevant aspects of our foreign trading, assistance and defense policies. Secretary Connally, in emphasizing the importance of dealing with this underlying deficit, noted that the immediate financing of this underlying deficit is clearly manageable in the context of the larger interests of defense of a stable monetary and liberal trading system.

At the present time, as a result of the large flows of money in search of higher interest returns, and more recently with speculative motivations, the dollar reserves of Germany -- and to a lesser extent a few other European centers -- have reached exceptionally high levels. The United States Treasury, in present circumstances, is prepared to assist in the orderly investment of these funds through special Treasury securities.

These views have been conveyed to the monetary authorities of other countries directly concerned, recognizing that decisions as to their exchange rates are properly a matter for those governments. The United States contemplates no change in its gold and foreign exchange policies.

oOo

[c. 5/7/71]

To: Chariman Burns Re: Market at 12:00

From: C. C. Baker

The bill market has improved in the wake of the Desk's outright cash purchases of $170 million of bills for System account; and rates are down 3 to 4 basis points. In coupon issues, the new when-issued securities are still under pressure but prices are about as they were earlier. The long end of the outstanding market has improved about 8/32 in price but the rest of the market is still unsteady. Federal funds are still trading at 4-7/8%.

The Desk now sees about $625 million of overnight Rp's that can be done and it is still requesting dealers to round up additional collateral for further Rp's. Withdrawals of outstanding Rp's now total about $250 million.

The Department of the TREASURY NEWS
WASHINGTON, D.C. 20220 TELEPHONE WO4-2041

MEMORANDUM TO THE PRESS: May 7, 1971

In response to further inquiries, Secretary of the Treasury John B. Connally said today that the Administration was continuing to carefully follow the speculative exchange market problem in Europe and remains prepared to cooperate fully with others to assist in stabilizing the situation.

The Secretary emphasized the United States contemplates no change in its own gold and foreign exchange policies.

Secretary Connally again expressed the view of the United States that maintenance of current parities could provide a basis for reopening the markets in various European centers. The Treasury is prepared to assist those few central banks receiving large amounts of dollars in recent weeks in the orderly investment of a portion of these funds through special Treasury securities.

The Secretary pointed out that consistent with orderly economic expansion, the U. S. was now making visibly more progress against inflation than its major trading partners overseas. This is the fundamental basis for continued confidence in the dollar at home and abroad.

Monetary authorities of other countries are aware of these views in reaching their decisions with respect to exchange rates and other policies.

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INTERNATIONAL MONETARY FUND
19th and H Streets N. W., Washington, D.C. 20431

PRESS RELEASE NO. 839

FOR IMMEDIATE RELEASE
May 9, 1971

The Federal Republic of Germany has informed the Fund that in view of the recent situation in foreign exchange markets, including large capital movements, for the time being it will not maintain the exchange rates for its currency within the established margins. The Netherlands government has informed the Fund that it has found it necessary to take similar action because of recent movements of foreign exchange and the action of the German authorities.

The two countries have given assurance that they will continue in close consultation with the Fund, and will collaborate fully in accordance with the Articles of Agreement. They have also given assurances to the Fund with respect to the resumption of the maintenance of the limits around par, in the interest of the smooth functioning of the international monetary system.

Belgium has notified the Fund that it is adapting the regulations concerning its free market for capital transactions with a view to stemming any large inflows of capital.

The Fund has given consideration to various ways of coping with the difficulties presently facing its members. In its consultations with members, and in its continuing work, the Fund will seek to maintain and strengthen the basic principles of the Bretton Woods system. The recent disturbances demonstrate the need to improve the international adjustment process and to bring about a better coordination among members with respect to their internal and external policies.

INTERNATIONAL MONETARY FUND

19th and H Streets N. W., Washington, D.C. 20431

PRESS RELEASE NO. 838

FOR IMMEDIATE RELEASE
May 9, 1971

After consultation with the Fund, the Government of Austria has changed the par value of the Austrian schilling, in accordance with the Articles of Agreement of the International Monetary Fund, from schillings 26 to schillings 24.75 per US$1 effective May 9, 7:00 p.m., Washington time.

The initial par value of schillings 26 per US$1 was established with the International Monetary Fund in April 1953 and the present change is being made under that provision of the Articles of Agreement of the Fund which entitles a member country after consultation with the Fund to make a change in the initial par value not exceeding 10 per cent.

Expressed in terms of gold and in terms of the U.S. dollar of the weight and fineness in effect on July 1, 1944, the new par value of the Austrian schilling is:

0.035 905 9	gram of fine gold per Austrian schilling;
866.250	Austrian schillings per troy ounce of fine gold;
24.750 0	Austrian schillings per U.S. dollar;
4.040 40	U.S. cents per Austrian schilling.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date May 12, 1971

To Chairman Burns

Subject:

From A. B. Hersey ABH

Attached is a first progress report, from Mr. Pizer, on efforts to glean some specific facts about recent speculative or hedging movements of funds from this country.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date May 12, 1971

To Mr. Hersey

Subject: Survey of liquid funds held abroad by corporations.

From Samuel Pizer SP

As I understand it, the Treasury (Mr. Schaffner) requested the OFDI to initiate some inquiries to major corporations to find out to what extent they had added to their liquid balances abroad between the end of April and May 7. This was done by telephoning on May 10 the twenty corporations with the largest allowables for liquid foreign balances. This was presented to the corporations as a voluntary inquiry not connected with compliance. A few were reluctant, but in any case OFDI expects to have replies from all of them by the end of the week and they will supply us with the results. The first reaction on the telephone by many companies was that they had not done anything like this.

We will get a copy of the questions that were asked. In general the companies were asked if they had increased foreign liquid balances held either directly or for their account by their subsidiaries in the first week of May, or whether they had made any prepayments of debt, and they were asked to break down their holdings as between dollars and foreign currencies.

In talking to the Treasury about this, I learned that the Treasury people are also interested in finding out what had happened to large payments made by petroleum companies to the oil-producing countries during April. Such payments approached $2 billion, and I said we would see what could be discovered from the banks about the disposition of these funds by the countries receiving them. I have given Fred Klopstock at the New York Reserve Bank the facts the Treasury has on oil royalty payments in April, and I asked him to look into the question.

cc: Mr. Solomon
Mr. Gemmill
Mr. Reynolds

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date May 14, 1971

To Chairman Burns

Subject:

From A. B. Hersey

ABH

CONFIDENTIAL (FR)

Attached is another report from Mr. Pizer on attempts to get more precise information about the outflows that were swelling the weekly balance of payments deficits through Wednesday the 5th.

We have still to get further reports on the OFDI survey.

cc: Mr. R. Solomon
Mr. Holland

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date May 14, 1971.

To Mr. Hersey

Subject: Flows of funds into Deutsche Marks.

From Samuel Pizer

CONFIDENTIAL (FR)

In the last few days the New York Bank (Scott Pardee) at our request has made some inquiries to try to discover some information about the source of funds going into Deutsche marks since the end of April. The first set of questions related to what the oil-producing countries might have done with their April tax receipts. A large part of those receipts are in sterling, and the Bank of England reports that they saw nothing out of the ordinary in the disposition of those receipts this year. Ordinarily the countries concerned have already incurred expenses in anticipation of the receipts so that they quickly move out of these accounts in any case. The Bank of England saw nothing different about transactions this year, and did not detect any extraordinary flows from these accounts into DM.

U.S. banks had very much the same impression, i.e., the countries do not ordinarily keep more than minimum accounts in the U.S., and on this occasion seem to be following practices similar to those followed at this time of the year in other years. In general, the banks felt that they were not likely to be able to detect any extraordinary transactions involving conversions of deposits held in the Euro-dollar market into DM, but they did not seem to have the impression that the oil countries' funds were taking that course.

Pardee reports that he and others at the New York Bank have a feeling from reports of Euro-market activity and from whatever conversations they have had with banks in the market that there were large conversions by U.S. corporations of U.S. funds into DM. In particular the U.S. banks reported picking up a very large amount of DM on Wednesday morning, having placed overnight orders. This was done partly for their own account to meet the commitments on earlier sales of DM to customers and partly directly for the account of customers.

The New York Bank has also discussed with the Bundesbank the possible sources of funds going into Germany, but up to now the Bundesbank reports that they have not been able to develop any useful information on this subject.

cc: Messrs. R. Solomon, Reynolds, Gemmill, and Bradshaw

MAY 14 1971

The Honorable William Proxmire
Committee on Banking, Housing and
Urban Affairs
United States Senate
Washington, D. C. 20510

Dear Senator Proxmire:

Your letter of May 3, attaching a reprint of an article by Milton Friedman, asks for comment on the issue of whether the substantial rate of growth in money supply over the past few months is related to "obsolete procedures" in carrying out monetary policy, with too much emphasis being placed on money market conditions and interest rates. I would say that the monetary growth experienced is not the product of a procedural problem, but rather that it reflects fundamental forces in the economy and has to be evaluated in relation to these forces.

The recent rapid growth rates in money, both narrowly defined to include currency and demand deposits (M_1) and more broadly defined to include also time and savings deposits at commercial banks other than large CD's (M_2), may be attributed mainly to two conditioning circumstances. First, particularly with respect to narrowly defined money, the recent rapid growth has reflected the temporary surge in demand for cash balances to accommodate enlarged transactions needs of the public resulting from the post-auto-strike rebound in economic activity. In the fourth quarter of 1970, because of the auto strike, the nation's gross national product valued in current prices rose at less than a 2 per cent annual rate; in the first quarter of 1971, with production recovering from strike-depressed levels, GNP rose at about a 13 per cent annual rate. Over the course of those two quarters, and roughly paralleling the swing in GNP growth rates, rates of increase in M_1 were around 3-1/2 per cent and 9 per cent, respectively.

While temporary variations in transactions demands for cash in the economy were central in explaining M_1 behavior over the past few months, it should also be noted that Treasury cash management practices have been a factor. There was a sizable net transfer of funds from the U.S. Government to private sectors late in the first quarter, indicated by a considerable drop on average in Government deposits from February to March. As often occurs, such net transfers led to a temporary enlargement of cash balances in private hands. Since peaking in early April, the outstanding amount of M_1 has declined on balance, in part reflecting replenishment of the Treasury cash balance.

The second principal explanation for rapid growth in money pertains mainly to M_2. In the early months of 1971, there was a sharp spurt in net inflows of time and savings deposits other than large CD's to banks. For the most part these are consumer-type time and savings deposits. We believe this spurt was largely the result of one-time transfers of savings by consumers out of market instruments, on which yields had dropped sharply during the fall and winter, to time and savings deposits at banks, whose yields had been maintained. According to preliminary estimates contained in the Board's quarterly flow-of-funds accounts, households sold or redeemed, net, about $17-1/2 billion of credit market instruments, principally U.S. Government securities, in the first quarter. In substitution, and reflecting also a continued high rate of net new personal saving, they added about $15 billion to their holdings of time and savings deposits at commercial banks and about $12 billion to deposits at nonbank savings institutions.

Most recently, net inflows to banks of consumer-type time deposits have slowed to more moderate proportions as many banks adjusted their offering rates down and as the amount of savings available for shifting was, in any event, worked off. This has led to a substantial moderation in the growth rate of M_2 following an unusually rapid 18 per cent annual rate of increase over the first quarter as a whole.

To slow down the growth in money--either M_1 or M_2--over the winter period of very rapid growth would have required the Federal Reserve to hold back on the provision of bank reserves. Total reserves of banks rose at about an 11 per cent annual rate in the first quarter, which accommodated--at the interest rates prevailing during the period--the temporary rise in demands for cash and the large shift by consumers in the forms in which their savings are held. If expansion in reserves had been at a slower rate, money market conditions would have been considerably tighter and, more broadly, both short- and long-term interest rates would have been higher than they were. As it turned out, the yield on new high-grade corporate bonds reached a low point in late January and has since risen by over one full per cent. And in short-term markets, Treasury bill rates were at lows in mid-March and have since risen, depending on maturity, by 60 to almost 100 basis points.

During the past several months, then, it has been necessary to weigh behavior of the monetary aggregates against the behavior of interest rates, and to assess them both in relation to the prospects for the strength of economic recovery and in light of the international position of the dollar. The Federal Reserve has not committed itself to a single financial indicator or objective in gauging monetary policy, but seeks instead to relate over-all financial conditions to the specific economic developments and prospects of the time. In the period under review, there were specific explanations for behavior of the aggregates which indicated that the rapid rates of growth would tend to be self-correcting. Moreover, since the economy was in the beginning tender stage of recovery, we judged that there was undue risk that any significant tightening in credit markets--particularly long-term markets--might hamper progress toward the expansion in economic activity and in job opportunities toward which we are all striving.

I hope these comments will prove useful to you. I recognize that there can be room for difference in analyses of the appropriateness of financial developments, even taking account of the economic environment in which they have occurred. The essential point, however, is that the recent rapid growth in the aggregates is not a matter of the procedures used in carrying out open market operations, but must be viewed in relation to credit market conditions generally, to an appraisal of what such conditions would have been if efforts had been made to reduce growth rates under the circumstances of the time, and to one's assessment of current economic conditions and economic prospects. I can assure you that we are watching the behavior of the monetary aggregates carefully, as well as the performance of the money and capital markets, and that we are prepared to move if that behavior should appear to threaten the prospects for orderly economic progress.

Sincerely,

(Signed) Arthur F. Burns

Arthur F. Burns

SHA:JCP:cmc
5/13/71

CHART 1 | STRICTLY CONFIDENTIAL (FR)

5/14/71

MONEY MARKET CONDITIONS

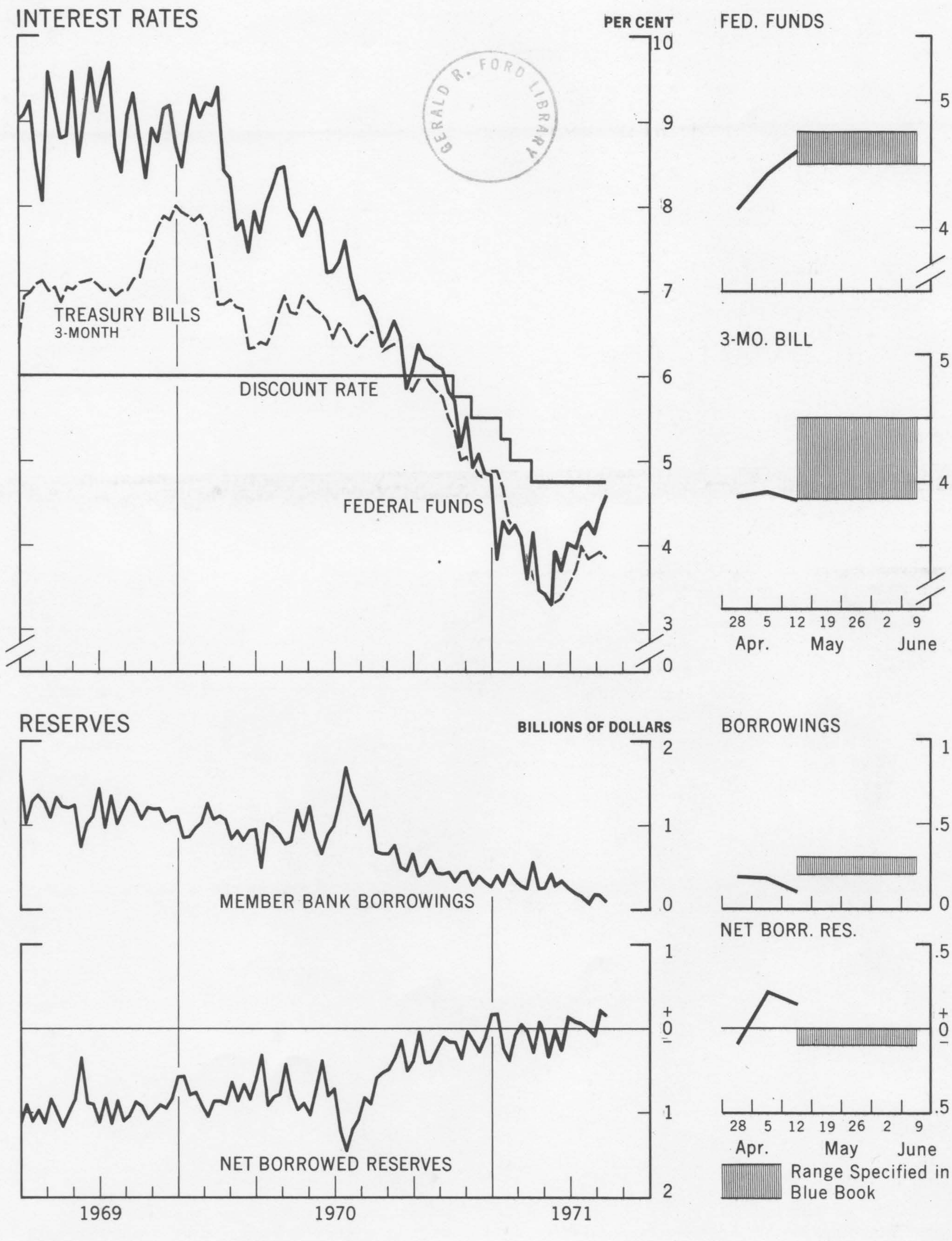
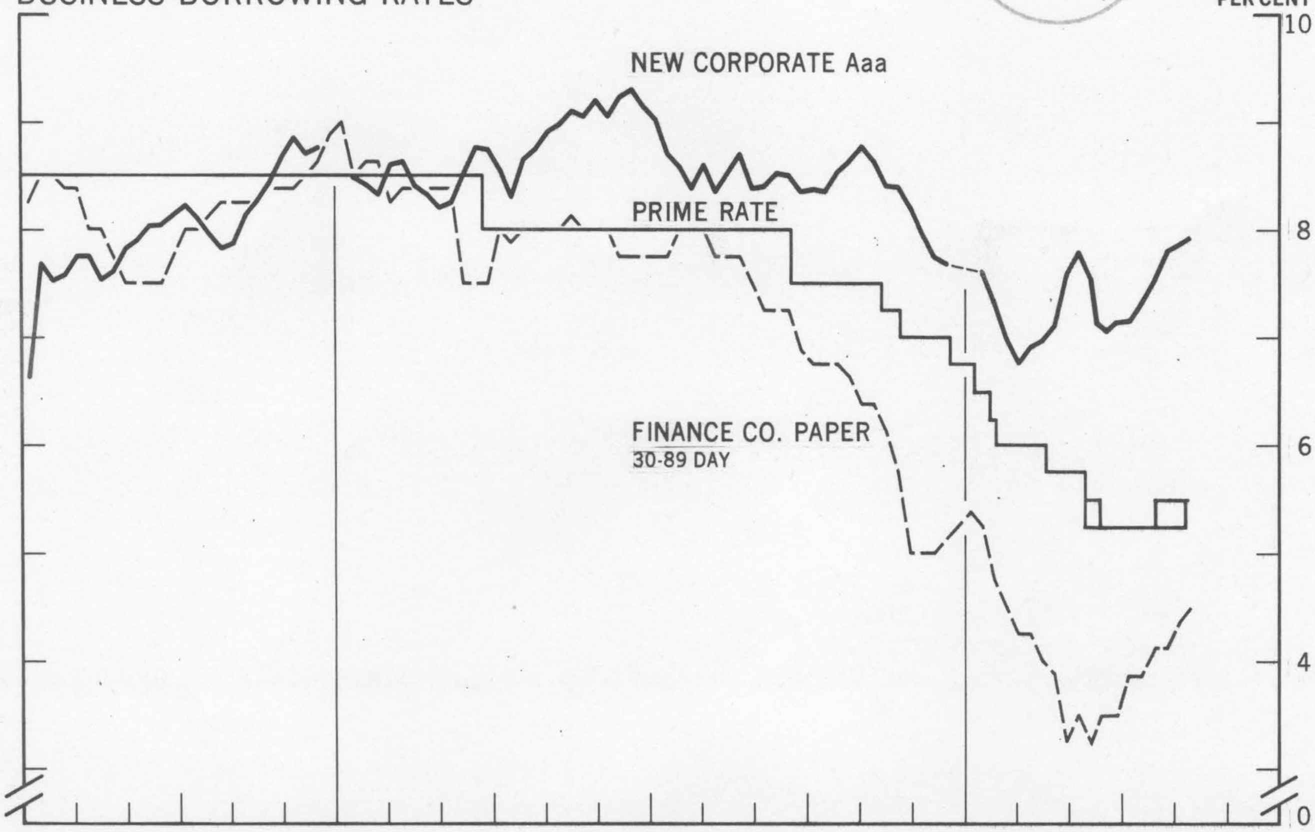


CHART 2 5/14/71

SELECTED INTEREST RATES

BUSINESS BORROWING RATES



OTHER LONG-TERM RATES

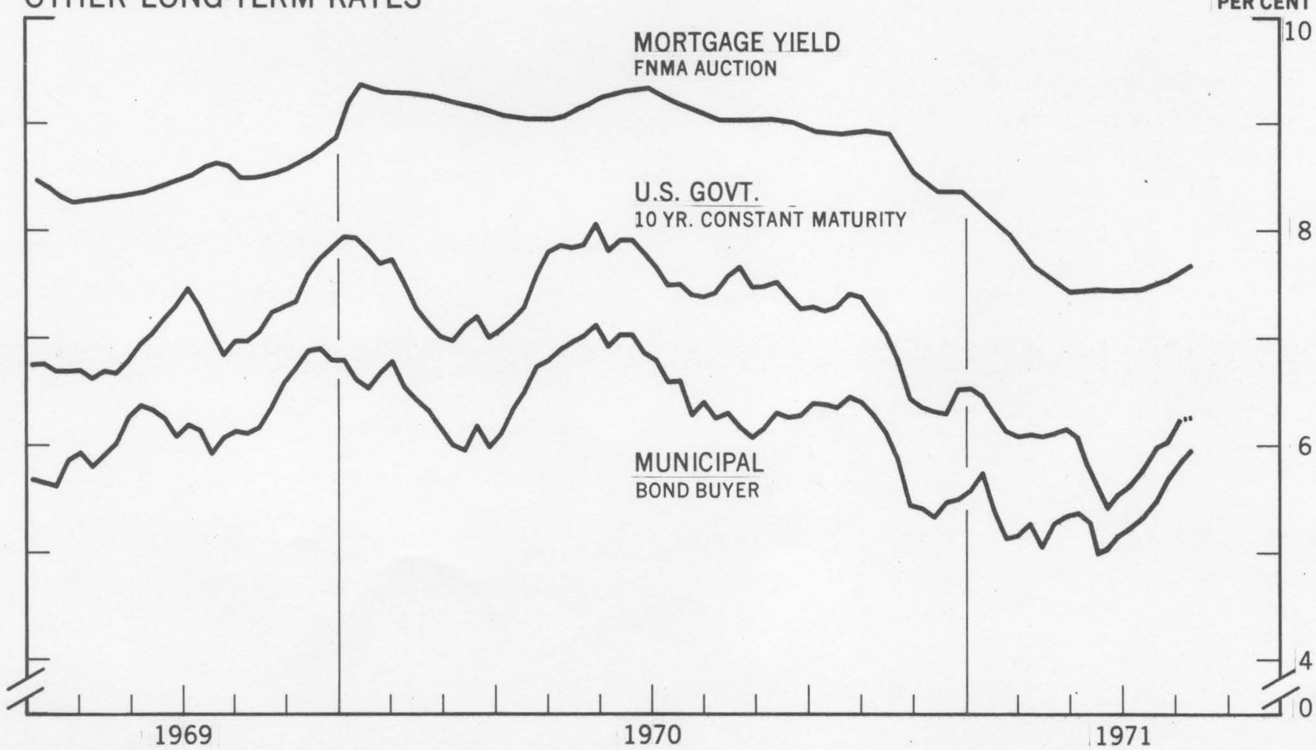
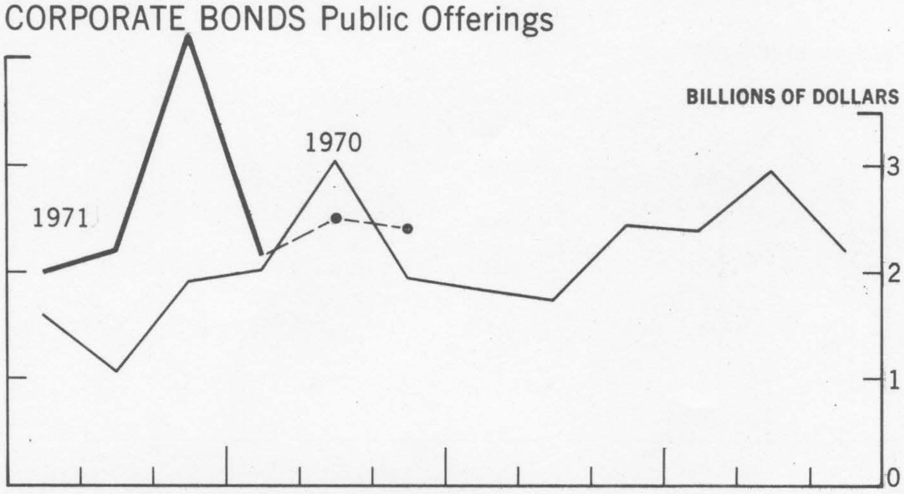


CHART 3

STRICTLY CONFIDENTIAL (FR)
5/14/71

SECURITY MARKET DEMANDS

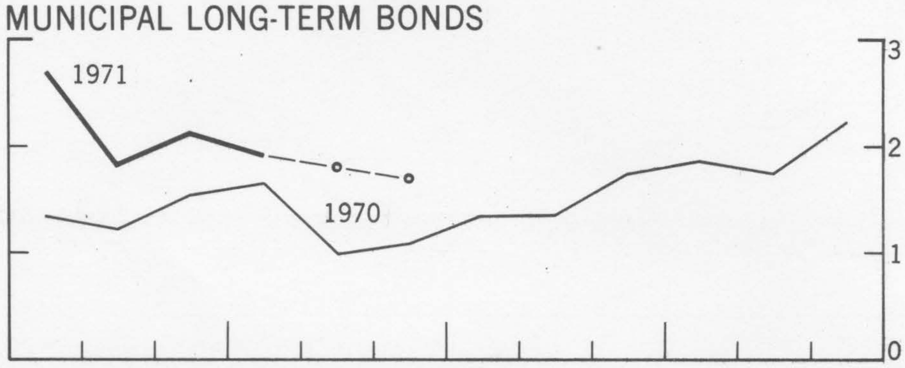
CORPORATE BONDS Public Offerings



CUMULATIVE BORROWING

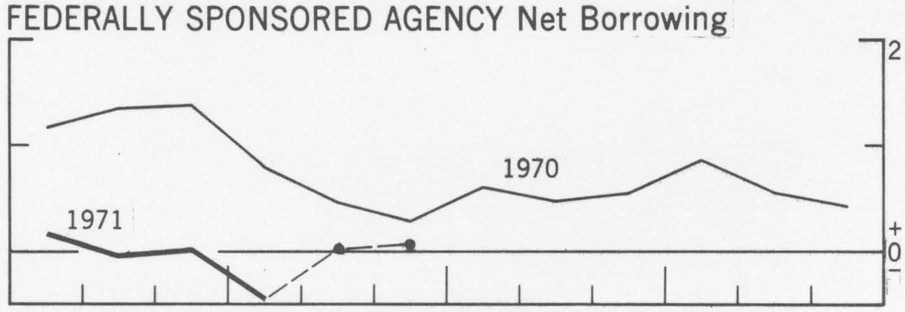
Through April
1970 6.5 Billion
1971 10.6 Billion

MUNICIPAL LONG-TERM BONDS



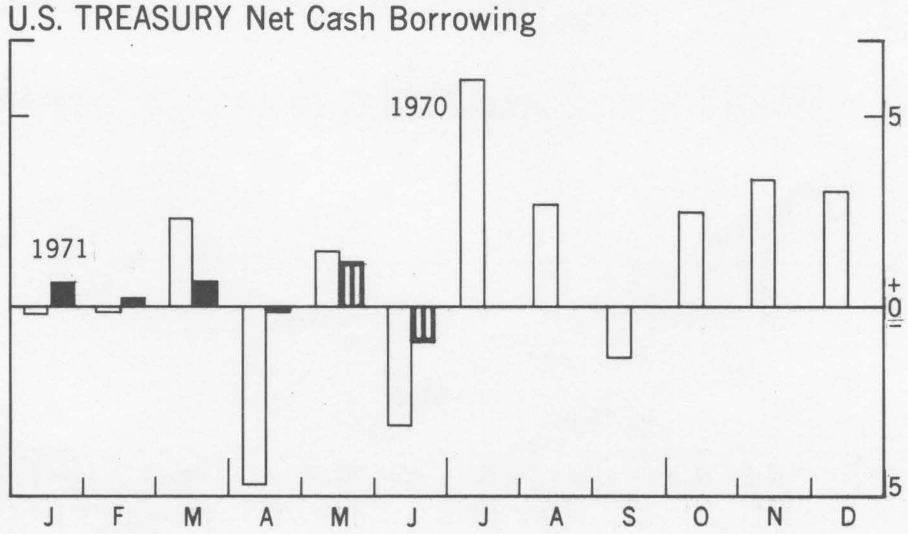
Through April
1970 5.7 Billion
1971 8.6 Billion

FEDERALLY SPONSORED AGENCY Net Borrowing



Through April
1970 4.6 Billion
1971 −0.3 Billion

U.S. TREASURY Net Cash Borrowing



Through April
1970 −2.7 Billion
1971 1.5 Billion p

Table 3

CONFIDENTIAL (FR)

MAY 14, 1971

SELECTED LONG-TERM INTEREST RATES

PER CENT

Period	Corporate Bonds: 1 New issue Aaa	Corporate Bonds: Moody's Seasoned: 2 Aaa	Corporate Bonds: Moody's Seasoned: 3 Baa	4 Bond Buyer's Municipal	5 U.S. Govt. (10-Yr. Constant Maturity)	6 FHA Mortgages (Secondary Mkt. Yield)	7 FNMA Auction Yields
1970: High	9.30	8.60	9.47	7.12	8.06	9.29	9.36
Low	7.68	7.48	8.59	5.33	6.29	8.40	8.36
1971: High	7.93	7.46	8.97	5.96	6.53	--	8.36
Low	6.76	7.06	8.34	5.00	5.42	--	7.43
1970: July	8.63	8.44	9.40	6.53	7.46	9.11	9.17
Aug.	8.48	8.13	9.44	6.20	7.53	9.07	9.03
Sept.	8.42	8.09	9.39	6.25	7.39	9.01	9.03
Oct.	8.63	8.03	9.33	6.39	7.33	8.97	8.91
Nov.	8.34	8.05	9.29	5.93	6.84	8.90	8.92
Dec.	7.80	7.64	9.12	5.46	6.39	8.40	8.43
1971: Jan.	7.24	7.36	8.74	5.36	6.24	--	8.16
Feb.	7.28	7.08	8.39	5.23	6.11	--	7.67
Mar.	7.46	7.21	8.46	5.17	5.70	7.32	7.44
Apr.	7.57	7.25	8.45	5.37	5.83	7.37	7.49
Mar. 5	7.79	7.12	8.40	5.37	6.07		7.43
12	7.54	7.20	8.47	5.28	5.82		--
19	7.14	7.26	8.50	5.00	5.61		7.45
26	7.08	7.25	8.47	5.03	5.42		--
Apr. 2	7.15	7.22	8.46	5.15	5.55		7.44
9	7.16	7.23	8.45	5.21	5.61		--
16	7.32	7.24	8.45	5.32	5.77		7.45
23	7.54	7.24	8.42	5.48	5.98		--
30	7.81	7.30	8.47	5.69	6.03		7.54
May 7	7.88	7.43 r/	8.52 r/	5.84	6.24 r/		--
14	7.93	7.46	8.57	5.96	6.28 p/		7.68
					6.65 5/4		

NOTES: Weekly data for Aaa corporate new issues, Moody's seasoned bonds and 10-year U.S. Government bonds are daily averages. Other weekly data are single-date figures. FNMA auction yield is the implicit yield in weekly or bi-weekly auction for 6-month forward commitments on Government underwritten mortgages.

FR 712 - C

MAY 14, 1971

Table 1

SECURITY DEALER POSITIONS AND BANK RESERVES

MILLIONS OF DOLLARS

Period	U.S. Govt. Security Dealer Positions		Other Security Dealer Positions		Member Bank Reserve Positions			
							Basic Reserve Deficit	
	1 Bills	2 Coupon Issues	3 Corporate Bonds	4 Municipal Bonds	5 Borrowings at FRB	6 Net ~~Borrowed~~ Free Reserves	(7) 8 New York	(8) 38 Other
1970 -- High	4,259	1,720	369	421	1,681	-1,451	-3,361	-5,619
Low	1,092	257	0	20	270	68	409	-3,076
1971 -- High	4,733	2,089	308	394	561	- 380	-4,779	-5,499
Low	*1,559	*1,066	22	96	84	202	-1,740	-3,006
1970 -- Apr.	3,466	692	102	140	865	- 687	-1,932	-4,628
May	1,428	949	32	119	924	- 765	-1,600	-3,306
June	1,509	562	45	221	907	- 735	-1,537	-3,608
July	2,365	626	45	112	1,317	-1,133	-1,473	-4,053
Aug.	2,630	1,435	90	135	881	- 707	-2,257	-3,957
Sept.	2,903	1,064	107	107	595	- 398	-1,853	-4,151
Oct.	2,724	1,120	98	242	468	- 274	-1,842	-4,282
Nov.	3,013	1,662	61	120	409	- 199	-2,340	-4,703
Dec.	3,739	1,636	221	279	348	- 84	-2,856	-4,713
1971 -- Jan.	3,555	1,767	82	188	377	- 140	-2,265	-4,485
Feb.	2,829	1,579	160	265	336	- 75	-2,568	-4,227
Mar.	2,972	1,252	110	191	312	- 120	-2,847	-3,927
Apr.	*3,268	*1,336	100	253	152p	24p	-3,752	-4,403
1971 -- Mar. 3	3,235	1,104	133	266	258	- 88	-2,300	-4,064
10	3,048	1,143	75	160	421	- 339	-3,205	-4,343
17	2,780	1,229	90	112	290	- 25	-2,764	-4,122
24	2,103	1,387	87	186	333	- 265	-2,973	-3,834
31	3,790	1,344	167	230	257	119	-2,566	-3,213
Apr. 7	4,733	1,484	164	360	197	80	-3,556	-4,473
14	3,613	1,252	58	202	150	58	-4,365	-5,499
21	*3,007	*1,261	128	251	84	- 3	-4,714	-4,593
28	*2,306	*1,318	48	197	177p	- 95p	-2,837	-3,491
May 5	*1,743	*1,304	90	125	175p	202p	-2,224p	-3,006p
12	*1,559	*1,066	55p	160p	98p	144p	-3,945p	-3,501p
19								
26								

NOTES: Government security dealer trading positions are on a commitment basis. Trading positions, which exclude Treasury bills financed by repurchase agreements maturing in 16 days or more, are indicators of dealer holdings available for sale over the near-term. Other security dealer positions are debt issues still in syndicate, excluding trading positions. The basic reserve deficit is excess reserves less borrowing at Federal Reserve less net Federal funds purchases. Weekly data are daily averages for statement weeks, except for corporate and municipal issues in syndicate which are Friday figures. *--STRICTLY CONFIDENTIAL

FR 712 - A

CONFIDENTIAL (FR)

MAY 14, 1971

Table 2

SELECTED SHORT-TERM INTEREST RATES

PER CENT

Period	1 Federal Funds	2 Dealer Loan Rate	3 60-89 day CD's	4 90-day Euro-dollar	5 30-89 day Finance Co. Paper	Treasury Bills 6 90-day	Treasury Bills 7 1-Year	8 Federal Agencies 1-Year
1970 -- High	9.39	9.98	7.88	10.34	9.00	7.92	7.57	8.75
Low	4.82	5.22	5.50	6.79	5.00	4.79	4.77	5.56
1971 -- High	4.59	5.41	5.38	7.36	5.25	4.87	4.73	5.56
Low	3.29	3.85	3.50	5.04	3.25	3.32	3.53	3.95
1970 -- Apr.	8.10	8.81	6.50	8.36	7.97	6.51	6.53	7.64
May	7.94	8.53	6.50	8.86	8.03	6.84	7.12	8.26
June	7.60	8.22	6.84	9.39	7.81	6.68	7.07	8.23
July	7.21	7.91	7.85	8.76	7.90	6.45	6.62	7.70
Aug.	6.61	7.28	7.68	8.19	7.69	6.41	6.55	7.58
Sept.	6.29	7.07	7.26	8.03	7.08	6.13	6.39	7.25
Oct.	6.20	6.67	6.63	7.94	6.63	5.91	6.23	6.99
Nov.	5.60	6.16	5.95	7.17	5.81	5.28	5.39	6.25
Dec.	4.90	5.36	5.53	7.25	5.15	4.87	4.84	5.65
1971 -- Jan.	4.14	4.93	4.85	5.92	4.69	4.44	4.40	5.18
Feb.	3.72	4.23	4.13	5.54	3.85	3.70	3.84	4.47
Mar.	3.71	4.21	3.60	5.11	3.45	3.38	3.60	4.06
Apr.	4.15	4.66	4.19	5.92	4.00	3.86	4.09	4.83
1971 -- Mar. 3	3.41	3.91	3.75	5.21	3.50	3.37	3.66	4.21
10	3.29	3.86	3.56	5.04	3.25	3.32	3.58	4.02
17	3.93	4.38	3.50	5.06	3.50	3.32	3.53	3.95
24	3.70	4.16	3.50	5.04	3.50	3.37	3.61	4.01
31	4.02	4.58	3.70	5.28	3.50	3.51	3.67	4.16
Apr. 7	3.98	4.53	3.88	5.64	3.88	3.71	3.72	4.32
14	4.20	4.66	4.13	6.08	3.88	3.99	4.08	4.60
21	4.27	4.78	4.25	5.84	4.12	3.84	4.09	4.90
28	4.14	4.68	4.50	6.03	4.12	3.88	4.32	5.04
May 5	4.41	4.94	4.63	6.41	4.38	3.92	4.46	5.27
12	4.59	4.99	4.63	7.36	4.50	3.85	4.49	5.46
19								
26								

NOTES: Weekly data are daily averages for statement weeks except for CD's and finance company paper which are Wednesday figures. CD rates are median offering rates posted by New York City banks.

FR 712 - B

FR 531
CONFIDENTIAL (FR)

WEEKLY REPORT OF MEMBER BANK BORROWING

(Averages of daily figures, in millions of dollars)

	Week ended		4 weeks ended		Year-ago data
	5-12-71	5-5-71	5-12-71	4-14-71	4 weeks ended 5-13-70
Total member bank borrowing:					
All member banks	98	175	134	235	863
Money market banks	59	81	53	25	484
Other reserve city banks	23	67	65	196	192
Country banks	16	27	16	14	187
Amount presently under administrative pressure:					
All member banks	22	49	57	194	75
Money market banks	-	-	-	-	46
Other reserve city banks	22	46	56	192	18
Country banks	*	3	1	2	11
Amount likely to come under administrative pressure next week, if borrowing continues:					
All member banks	-	-	*	*	22
Money market banks	-	-	-	-	10
Other reserve city banks	-	-	-	-	-
Country banks	-	-	*	*	12
Amount accounted for by frequent borrowers:					
Indebted in 10-13 of past 13 weeks:					
All member banks	22	79	57	194	22
Money market banks	-	-	-	-	-
Other reserve city banks	22	77	56	192	-
Country banks	*	2	1	2	22
Indebted in 7-9 of past 13 weeks:					
All member banks	40	*	11	1	126
Money market banks	39	-	10	-	25
Other reserve city banks	-	-	-	-	57
Country banks	1	*	1	1	44

NOTE: Amount of borrowings brought under administrative pressure is dependent on a variety of circumstances, only one of which is the duration of the borrowings. The two sets of figures are both included as complementary indicators of the composition of total member bank borrowing, and neither the aggregate amounts nor necessarily the individual banks included will completely coincide.

* Less than $500,000.

DIVISION OF FEDERAL RESERVE
BANK OPERATIONS
May 13, 1971

The Department of the TREASURY NEWS
WASHINGTON, D.C. 20220 TELEPHONE WO4-2041

FOR RELEASE UPON DELIVERY May 17, 1971

STATEMENT BY THE HONORABLE JOHN B. CONNALLY
SECRETARY OF THE TREASURY
BEFORE
THE SENATE FINANCE COMMITTEE
SUBCOMMITTEE ON INTERNATIONAL TRADE
MONDAY, MAY 17, 1971, 10:00 A.M.

I congratulate the Senate Finance Committee on establishing this Subcommittee on International Trade, and I welcome this opportunity to discuss with you the broad aspects of our international economic policies.

Mr. Chairman, in March you submitted to the Finance Committee a very thoughtful report concerning trade policies in the 1970's. You indicated that we are at a watershed. You said that in the future we must have both a change in direction and a change in emphasis in pursuing our foreign economic policy objectives. And you also stated that those changes in direction and emphasis had to be accompanied by a corresponding change in the means of pursuing our objectives.

(MORE)

C-52

I agree strongly with all of these conclusions. And in this prepared statement, I would like to take just a few minutes to underline that agreement, and to capsule the type of actions necessary both at home and abroad if we are to succeed in this important effort.

The road to good international economic relations is not a one-way street -- no nation, regardless of power or prestige, can or should "call all the shots" for the free world community. Nor can we or others, in building a world order, expect to rely for long on the goodwill or largess of friends. We need to recognize that lasting cooperation among nations depends not on friendship in the personal sense, but on the solid base of national strength and national interest. By taking a long and broad view of our interests, and building on the elements of common needs and aspirations, we can expect strong allies in our endeavor to maintain a flourishing world economy.

To play our proper role in the new age to which you refer, there are things that we must do at home. Just as important, there are steps that must be taken by us and by our trading partners in building better trading relationships abroad.

For many years we had the luxury of competing with economies still recovering from war. We prospered during this period. Now, circumstances have changed in the world. We must change to meet these new circumstances. A generation of ease and affluence enjoyed by labor and business alike -- a period when our strength was so apparent that erosion in our competitive position was almost unnoticed -- is over.

As we enter the 1970's, the relative economic strength of our major trading partners is abundantly clear. The European Economic Community is now the world's largest trading bloc, with large and persistent trade surpluses. The prospects are that its membership and economic base will soon be further expanded. Japan has achieved a truly remarkable rate of growth. It now records the second highest Gross National Product and among the largest trade and balance-of-payments surpluses in the free world.

The simple fact is that in many areas others are out-producing us, out-thinking us, out-working us, and out-trading us. Analysis of trends in our balance of payments underlines this.

I do not refer just to the statistics for the first quarter of 1971, to be released today. Those results are bad. They depict a deficit of over $5 billion on the official settlements basis for the three months alone. The liquidity deficit exceeded $3 billion.

Clearly, that level of deficit is not sustainable. However, we should clearly recognize that the major cause of these extraordinary dollar outflows is transitory -- interest rates here which are lower than those in Western Europe. That imbalance will be largely corrected as economies move back into phase.

What disturbs me more than the first quarter deficit is the underlying trend in our trade and current account position. Our trade surplus rose in the first quarter, but still ran below the rate for 1970 as a whole. More importantly, it remains far below the levels of the early 1960's, and below the amount we need to achieve an equilibrium in our balance of payments.

To keep pace in this world economy, our first task is to attend to our own economy. We must restore the stable, noninflationary growth that was disrupted by the domestic financial policies of the late 1960's.

We are well on the way down this difficult road. Our strategies for further containing inflation, while raising output and reducing unemployment, are working. In particular, we have begun to restore the base for a stronger international position; last year, unit labor costs in the U.S. rose only one-third as much as the average of our major competitors. This is heartening evidence of fundamental progress.

But the journey is far from over. We cannot afford to sit back and count on poor performance abroad. Thus, the remaining challenge before us at home is plain.

Our domestic economic strategy of balanced and sustainable recovery will help rebuild our trade surplus -- but only slowly. In addition, we cannot hope to achieve a full measure of success unless markets are open to us and unless we are able to compete fairly with our trading partners abroad.

Indeed we must paint on a larger canvass than trade alone. We are now at a decisive point in our economic affairs. The challenge in foreign economic policy for the 70's involves three elements. First, the necessary mutual security arrangements for the free world must be maintained in full concert with our allies, with a fair sharing of the burden. Second, multilateral coopera-tion must be broadened in the financial and development assistance areas. Third, the efforts to foster increased competitiveness in our economy must be actively pursued in the context of fair and liberal trading arrangements.

It is this last area that seriously concerns this Committee today. I believe we have legitimate complaints about some of the practices of other nations -- now in a strong position -- that have the effect of blunting our competitive effort. Twenty years -- even a decade -- ago, these practices might have been understandable. I believe the strength of other nations should now permit new initiatives to break down these barriers.

I do not want to be misunderstood. I am not pleading with other nations to reduce barriers and open markets in return for what the people of the United States have done for them in helping to recover from the ravages of World War II. My point is simply that today we are in a different world -- and there is a common interest in achieving new and balanced trading relationships.

Mr. Chairman, there is another area -- in addition to efforts by our Government and by governments abroad -- in which a new approach is necessary. I refer to the private sector.

Bluntly stated, the statesmanlike leadership that the President of the United States has evidenced in dealing with this nation's foreign and domestic problems has not been correspondingly matched in the private sector. This is a time for the private sector to do everything possible to hold down the rise in labor costs, to avoid unnecessary increases in interest rates, and to speed the return to price stability.

It is time for Americans to realize that stronger efforts have to be made to raise productivity. We find it too easy to blame the Government when in fact we are all part of the factors which govern the course of our economy. Labor and business have a bigger stake, a larger voice, and a stronger hand in this economy than Government does. It is now time for them to use that strength constructively.

Our trading position shows that we will have to work harder just to maintain our position. This nation -- its industry and its labor -- must help redress the decline in our competitive position and improve our economic performance in foreign markets. Government should help when necessary and appropriate with credit support, by fair taxation, and by promoting our technological leadership. This is why the Administration has strengthened the Export-Import Bank activities. This is why we will resubmit our proposal for a Domestic International Sales Corporation, changing tax treatment of exports in a way to awaken our companies to the opportunities abroad. And this is why I am distressed at the reduction in federal expenditures on research and development.

Now, I realize that there may be a tendency to think, or at least hope, that our international financial problems can be taken care of by some sort of monetary magic. Nothing could be further from the truth. Money itself cannot produce, increase efficiency, or open markets abroad. Our monetary system functions well only as the economy as a whole functions well. A dollar is not just a piece of black and green paper with George Washington on one side and a big ONE on the other. That little piece of paper represents and reflects the economic vitality -- or lack of it -- of this country.

When this Administration calls upon businessmen, labor leaders, and bankers to put their respective shoulders to the wheel and work together for the common good, we may run the risk of being described as old-fashioned, for what I am calling for is a return to the principles of hard work and responsibility -- principles that are reflected in high and rising levels of productivity. Productivity, in its broadest sense, is truly "the name of the game" in the hard competitive world of international trade. I do not at all mind being called old-fashioned when the standard of living of the American people -- their personal and economic security -- is at stake.

At the same time, the private sector, from whom I am calling for renewed effort, has every right to expect and certainly should receive a more attentive interest and a more insistent effort in protecting our economic and financial interests around the world.

oOo

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date May 17, 1971

To Mr. Axilrod

Subject: Immediate Price Effects of Monetary Disturbances this Month

From Mrs. Smelker MS

Futures price fluctuations for non-precious metals were not much affected by the monetary disturbances this month. Copper futures strengthened temporarily--the increase in prices on May 5 was attributed to monetary developments, but this was followed by a resumption of declining futures prices. Copper spot prices fluctuated but in general continued to move down.

Agricultural futures showed little effect, as would be expected. Wheat, corn and soybeans futures apparently strengthened temporarily after the Mark was floated, but other factors may also have been important.

Precious metal futures strengthened this month--particularly gold and platinum.

Attachment.

FR 201
(1-60)

Futures Prices of Selected Commodities

1971

Commodity	Month of Maturity	Apr 30	May 3	May 4	May 5	May 6	May 7	May 10	May 11	May 12	May 13	May 14
Chicago Wheat												
	May	158 3/4	157 7/8-3/4	158 1/4	160 5/8-1/2	158 5/8-1/2	158 1/2-5/8	158 7/8-3/4	158 3/4-1/4	160 5/8	159 3/4-7/8	159 1/2
	July	151 3/4-5/8	150 1/2	150-149 7/8	150 3/4-1/2	151 1/2-3/8	151 3/8-1/2	150 1/8-150	150-150 1/8	151 1/2	150 7/8	149 3/4
	Sept	153 3/8-1/4	152 1/4	151 1/4	152 1/8	152 7/8	153 1/8	151 1/4-1/8	151 1/4	152 1/2	151 7/8	150 7/8
	Dec	157 3/4	156 1/2	155 1/4	156	157 1/4	157 1/8	155 1/4-1/8	155 1/4	156 1/2-5/8	155 3/4	154 3/4-7/8
Corn												
	May	143 1/8-1/4	143 1/2-5/8	141 3/4-142	142 7/8-143	144 7/8	144 1/4-3/8	144-144 1/8	144 3/8-1/2	145 7/8-146	145 1/2-5/8	148 7/8-149
	July	144 1/2-3/8	144 3/8-1/2	142 7/8-143	143 5/8-3/4	144 3/4-7/8	143 3/4-7/8	143 1/8-1/4	143 1/8-1/4	144 1/8-144	143 7/8-3/4	145-145 1/8
	Sept	143 3/8-1/2	143 1/4-3/8	141 5/8	141 7/8-142	142 7/8-143	141 5/8-3/4	141	140 1/2	140 7/8-141	140 3/4	141 5/8
	Dec	140 3/8-1/4	139 7/8-3/4	137 7/8-3/4	137 3/4-5/8	138 1/2-1/4	137-137 1/8	136 1/4	135 7/8-5/8	136 5/8-1/2	136-136 1/8	137 1/4-3/8
Soybeans												
	May	292-292 1/2	291 5/8-3/8	292 1/8-1/4	296 1/8-1/4	297-296 3/4	295-294 7/8	295 5/8	297 5/8-1/2	297 7/8-298	296 1/8-296	297 3/4
	July	295 7/8-1/2	295 1/4-3/8	295 3/4-7/8	300-299 3/4	300 1/8-3/8	298-297 3/4	298 3/8-1/2	299 3/4-1/2	300 1/8-1/4	298-297 3/4	298 3/4-5/8
	Aug	295 3/4-1/2	295-295 1/8	295 3/8-1/4	299	299 1/4-3/8	296 3/4	297 3/8	298 3/4-7/8	299 1/8	296 5/8	297 5/8-3/4
	Sept	289 1/4-1/8	289 1/4	289 1/8-289	293 1/4-3/4	293 1/2-3/4	291 3/4-7/8	292 3/4	293 3/8-1/2	294 1/8-1/4	292 1/8	292 7/8
	Nov.	283 3/8-1/2	283 5/8-3/4	283 1/2	287 1/2-3/4	289 1/8-289	287 1/8-1/4	287 3/4-288	288 1/4-1/2	289 1/8-3/8	287 3/4-5/8	288 1/4-288 3/8
Cocoa N.Y.												
	May	24.45	24.00	23.65	23.49	23.79	23.36	23.53	23.20	22.90	23.30	22.88
	July	23.34	22.75	22.40	22.70	22.55	22.29	22.47	22.30	22.05	22.45	21.93
	Sept	23.85	23.28	22.95	23.24	23.06	22.82	22.97	22.80	22.56	22.90	22.48
	Dec	24.35	23.75	23.45	23.71	23.60	23.36	23.48	23.30	23.00	23.44	22.92
GOLD (London, 3P.M.)		39.70	39.43	39.65	40.10	40.30	39.775	39.84	40.20	40.45		41.20

1

FR 201
(1-60)

~~1977~~ Futures Price Movements
May 3 to May 14, 1971

N.Y. MERCANTILE EXCH.

Commodity / Month of Maturity		Apr. 30	MAY 3	MAY 4	MAY 5	MAY 6	MAY 7	MAY 10	MAY 11	MAY 12	MAY 13	MAY 14
PALLADIUM	June	34.90	33.80	34.50	35.00	35.00	35.00	35.00	35.00	35.00	35.00	35.00
	Sept	35.00	34.75	34.75	34.75	34.75	35.00	34.75	34.75	34.75	34.75	34.75
PLATINUM												
	July	102.40	101.50	103.70	106.50	106.90	106.10	105.30	106.50	107.00	109.50	110.90
	Oct	103.80	103.40	105.90	108.90	108.80	107.90	106.90	107.90	108.50	110.70	111.70
	JAN	105.80	105.40	107.60	110.60	110.50	109.50	109.60	109.50	110.00	112.80	113.30
	APR	107.70	107.00	109.70	112.50	112.10	111.30	111.00	111.00	111.50	114.50	115.50
	July	109.50	109.00	110.70	114.00	114.00	113.00	112.00	113.00	113.50	116.00	117.30
	Oct		109.50		116.50	116.60	115.00	113.00	115.00	116.00	117.50	119.50
NICKEL												
	June	130.00	130.00	—	130.00	130.00	130.00	~~130.00~~ 130.00	130.00	130.00	—	—
SILVER												
	MAY	167.80	164.50	167.50	170.10	169.50	169.00	167.70	167.40	168.10	170.70	168.70
	June	169.00	156.60	168.50	171.10	170.50	169.90	168.60	168.30	168.40	171.30	169.30
	July	170.20	166.70	169.60	172.20	171.60	171.00	169.60	169.30	169.90	172.30	170.30
	Sept	172.60	169.00	171.90	174.50	173.90	173.30	171.90	171.60	172.20	174.60	172.60
	Dec	176.10	172.40	175.40	178.00	177.40	176.80	175.40	175.10	175.70	178.10	176.10
	JAN	177.20	173.40	176.50	179.20	178.60	178.00	176.60	176.30	176.90	179.30	177.30
	MAR	179.50	175.80	178.80	181.50	180.90	180.30	178.90	178.60	179.20	181.60	179.60
	MAY	181.80	178.10	181.10	183.80	183.30	182.70	181.20	181.10	181.60	184.00	182.00
	July	184.10	180.40	183.40	186.10	185.60	185.00	183.50	183.30	183.90	183.30	184.40
	Sept	187.40	182.70	185.70	188.40	187.90	187.30	185.80	185.60	186.20	188.70	186.70
Copper												
	MAY	53.40	53.10	51.90	52.30	52.05	52.50	51.60	49.90	50.35	50.00	50.60
	July	54.10	53.80	52.60	53.00	52.65	53.05	52.15	50.50	50.90	50.50	51.05
	Sept	54.55	54.35	53.20	53.55	53.15	53.55	52.60	50.90	51.35	51.05	51.50
	Oct	54.65	54.55	53.30	53.60	53.25	53.65	52.80	50.95	51.40	51.10	51.55
	Dec	54.65	54.45	53.30	53.60	53.25	53.65	52.60	50.90	51.40	51.15	51.60
	JAN	54.65	54.45	53.30	53.60	53.25	53.65	52.60	50.90	51.45	51.20	51.65
	MAR	54.60	54.40	53.25	53.55	53.25	53.65	52.60	50.90	51.50	51.20	51.65
	MAY	54.55	54.35	53.25	53.55	53.25	53.65	52.60	50.90	51.50	51.20	51.65
Tin												
	MAY	164.00	163.00	163.00	164.00	163.25	163.50	162.75	163.25	163.25	163.50	163.75
	SEPT	164.00	163.00	163.50	164.00	163.25	163.50	162.75	163.25	163.25	163.50	163.75
LME Copper wirebar	BID			480.00	484.50	474.0	482.50	473.00	466.50	457.00	463.50	466.00
	SPOT	487.00	492.50									
	Forward	497.50	502.50	490.00	494.00	484.0	492.50	483.00	476.00	467.00	473.00	475.00

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date May 17, 1971.

To Chairman Burns

Subject: Information Requested at May 14, 1971 Board Meeting.

From Peter Treadway

Enclosed are the following:

1. A graph showing the relative performance of selected stock price indices from January 1968 through April 1971. This graph gives a broad view of stock price movements over the last three years.

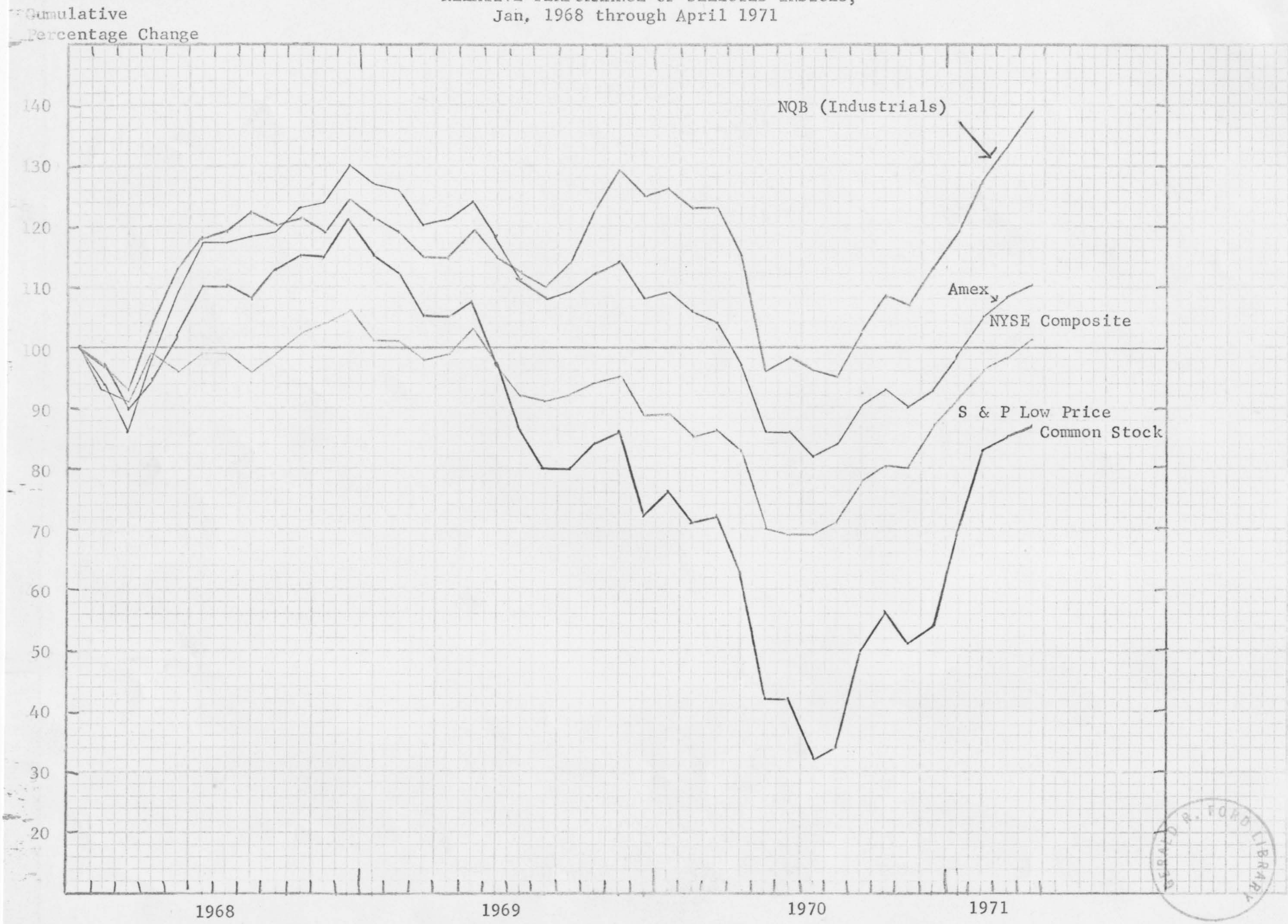
2. A graph showing the relative performance of selected stock price indices from July 1970 through April 1971. This graph presents clearly the relative recovery of each index from its average monthly 1970 low.

Note that both graphs plot indices by cumulative per cent changes over the period specified. We chose this method instead of plotting actual monthly values on log paper because this achieves virtually the same result and in this case made the graph easier to read.

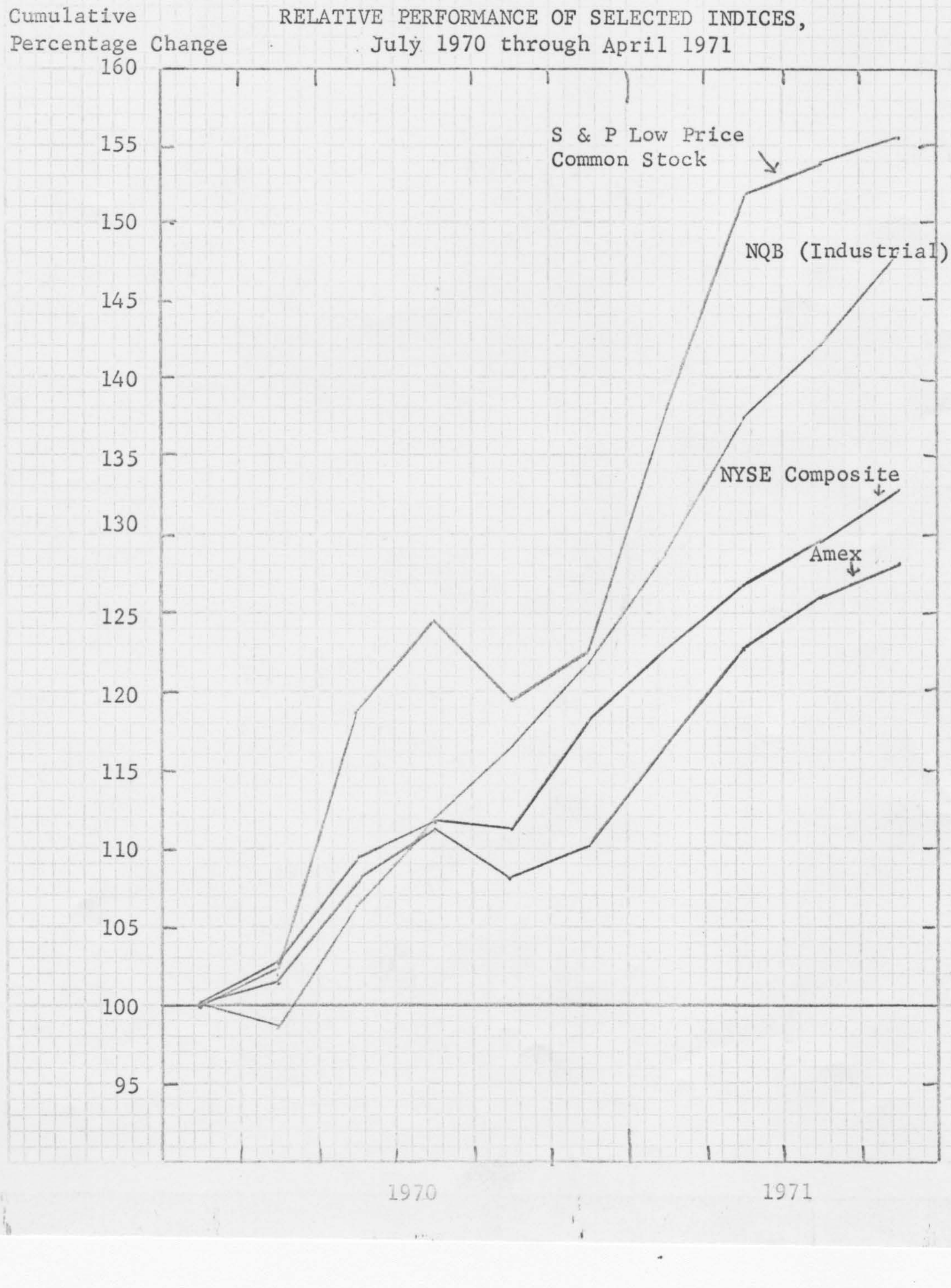
3. A chart showing net purchases, gross purchases and gross sales of U.S. stocks by foreigners. This chart contains the latest Treasury data available and shows that stock trading volume accounted for by foreigners had increased substantially through March but that foreigners in early 1971 had to a small extent become net sellers of U.S. securities.

FR 730

RELATIVE PERFORMANCE OF SELECTED INDICES,
Jan. 1968 through April 1971



RELATIVE PERFORMANCE OF SELECTED INDICES,
July 1970 through April 1971



FOREIGN PURCHASES & SALES OF U.S. STOCKS

(In $ millions)

		STOCKS		
		Net Purchases	Gross Purchases	Gross Sales
Year:	1968	2,270	13,118	10,848
	1969	1,487	12,429	10,942
	1970	623	8,927	8,304
1970	January	(43) r	775	818 r
	February	(13) r	756 r	768
	March	(41)	855 r	895 r
	April	4 r	732 r	728 r
	May	(200)	628	829
	June	63 r	626	563 r
	July	52 r	545 r	493 r
	August	104	535	432
	September	225	829	604
	October	158	948	790
	November	98	619	521
	December	216	1,078	862
1971	January	130	999	869
	February	(32)	1138	1170
	March/p.	(36)	1072	1108

/p. New York District only, representing 90% of the total.

r = revised

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

DATE 5/20

TO Chairman Burns

FROM ROBERT SOLOMON

The attached memo spells out the case for having central banks reverse their Eurodollar placements directly rather than through the BIS.

RS

Attachment.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date May 20, 1971

To Mr. Robert Solomon

From Robert F. Gemmill

Subject: Use of BIS in shifting foreign central bank funds to the United States

~~CONFIDENTIAL~~ (FR)

If it is desirable to secure withdrawal of foreign central bank funds from the Euro-dollar market, it would appear possible to accomplish that result without involving the BIS.

1. Any withdrawal would have to be spread over a considerable period of time so as not to precipitate a crisis in the Euro-dollar market -- or boost Euro-dollar rates sufficiently to contribute to a sizable outflow of U.S. capital in a short period of time.

2. Thus, foreign central bank balances withdrawn from the Euro-dollar market would be invested in the United States over a period of time; maturities could be staggered, so that the average time remaining to maturity of the investments in a foreign central bank's portfolio would always be about half that of the original maturity of the individual investments.

3. At current rates, a foreign central bank could have a portfolio of 90-day CD's (average maturity 45 days) with an average yield of 5 per cent, or a portfolio of 30-59 day CD's (average maturity 15-30 days) with an average yield of about 4-1/2 per cent.

The foreign central bank could obtain somewhat greater liquidity (for any given average maturity of portfolio) if it invested in Treasury bills rather than CD's, and a somewhat lower yield (3-month bills currently about 4.4 per cent, and 30-day bills about 4 per cent.)

4. Foreign central banks have reportedly invested funds in 3-month deposits with the BIS at 4-3/4 per cent yield with a 2-day call. The yields available on U.S. assets come quite close to the yields on deposits with the BIS, and it should be possible to persuade foreign central banks that the small yield advantage that individual banks might obtain on BIS deposits was outweighed by the adverse effects of the practice in fostering a multiple expansion of reserves.

5. If foreign central banks require greater liquidity on their dollar holdings in the United States than would be provided by staggered maturities -- e.g., if the two-day call provision that they reportedly have on deposits with the BIS is an important element in their investment decisions -- this could be provided through use of the Federal Reserve swap network.

6. The BIS itself uses the swap line to obtain liquidity, and any proposal that involves use of the BIS as an intermediary therefore implicity (if not explicitly) involves use of the Federal Reserve swap network as an ultimate source of liquidity. In principle, it would be preferable to provide liquidity directly to foreign central banks through the swap, rather than using the swaps to support the BIS in a profit-making operation. Why not eliminate the middle man?

cc: Hersey, Reynolds, Pizer, Bradshaw

[c. 8-71?]

Exchange Rate Changes Required to Achieve Balance of Payments Targets

(In billions of SDRs)

	Current Account Balance for 1970, Cyclically Adjusted 1/ (1)	Trend Adjustment 2/ (2)	(1) + (2) (3)	Current Account Target (1970) 3/ (4)	Adjustment Needed to Reach Target (4) - (3) (5)	Required Exchange Rate Change Relative to U.S. Dollar 4/ (in per cent) (6)
Belgium-Luxembourg	0.7	0.0	0.7	0.2	-0.5	10.0
France	0.0	-0.2	-0.2	0.3	0.5	7.3
Germany	3.8	0.8	4.6	1.8	-2.8	13.4
Italy	1.1	0.0	1.1	0.8	-0.3	9.4
Netherlands	-0.3	0.2	-0.1	0.2	0.3	7.3
United Kingdom	1.0	-0.2	0.8	0.9	0.1	7.2
Canada	1.1	0.2	1.3	-0.2	-1.5	12.1
Japan	3.3	1.0	4.3	1.6	-2.7	15.0
United States	-1.2	-2.0	-3.2	4.8	8.0	0.0
Other OECD	0.0	0.2	0.2	-0.9	-1.1	9.3

1/ Goods, services, and private remittances. Based on OECD paper CPE/WP3(71)13, Table 2, and data supplied by OECD Secretariat; 1970 current balance for U.S. lowered by $0.5 billion in accordance with latest, revised U.S. estimates.

2/ Rough projection of change from 1970 to 1972 in column (1) figures in the absence of exchange rate changes. Figures expressed in 1970 pric[illegible]

3/ Based partly on OECD estimates of "reasonably balanced position in 1970" (CPE/WP3(71)13, Table 3), and partly on IMF staff estimates of "normal" net flows of capital and aid.

4/ Calculated on the basis of the IMF staff's multilateral exchange rate model. Changes measured from parities prevailing before May 30, 1970.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date August 9, 1971

To Chairman Burns

Subject: Dale Proposal Regarding Exchange Rate Realignment.

From Robert Solomon

~~S E C R E T~~

The attached paper written by Bill Dale, sets out a proposal for achieving a sizable realignment of exchange rates --aimed at producing a large U.S. surplus--and doing so without raising the official price of gold. I understand that this paper has been seen by Secretary Connally and Peter Peterson.

RS

Attachment.

DECLASSIFIED
AUTHORITY Fed. Res. Ltr. 11/16/82; State guidelines
Treasury Ltr. 8/22/06
BY [illegible] NARA, DATE 9/29/09

Attachment A

~~SECRET~~

Exchange Rate Realignment and Related Matters

The points made below attempt to lay out some essential elements of a scenario which would be aimed at accomplishing a major realignment of exchange rates while still observing certain of the unavoidable constraints on possible action by the United States and taking account of what may be legally and practically feasible in the existing international monetary system.

A. This approach would concentrate action within a period of two weeks at the longest (it should, of course, be made as short as feasible)-- the week prior to, and the week of, the IMF Annual Meeting this year. In the week prior to the weekend when the IMF Governors arrive in Washington, the United States would discontinue the "free" sale of gold and SDR's against dollars and would close its exchange markets. Other major countries would presumably do the same. The aim would be to reopen exchange markets within two weeks. During the week preceding the Annual Meeting, the U.S. authorities would seek Congressional action permitting the United States to initiate and approve a major realignment of exchange rates. The type of Congressional action to be sought is shown in Attachment 1. The essence of the approach would be that the President and other officials delegated by him would be authorized to propose and agree to a combination of a uniform change in par values and a change in the par value of the U.S. dollar in such a manner that the official U.S. dollar price of gold would at no time exceed $35 per ounce. This would be sought by an initial step comprising a uniform appreciation of the currencies of all Fund members so that the official U.S. dollar price of gold would be below $35 for an interim period of a few days. The percentage rates of uniform appreciation corresponding to various gold prices down to $28 per ounce are shown in Attachment 2. After a uniform appreciation of the appropriate magnitude (say, up to 25 per cent) the United States would propose, and the Fund would agree to, an individual depreciation of the U.S. dollar back to the point where the official price of gold would be $35.

B. Having obtained the necessary Congressional legislation (which is formulated in Attachment 1 in general terms so that similar exchange adjustments could also operate in the future) the United States would have, beginning with the weekend preceding the Annual Meeting, the various groups of foreign officials at hand with which international

~~SECRET~~

negotiations would be orchestrated. These would include, in addition to the full IMF Board of Governors itself, the G-10 Deputies, the G-10 Ministers and Governors, the EEC officials and the IMF Board of Directors. The United States would propose that a uniform appreciation of, say, 25 per cent, up to an official gold price of $28 be approved by the Fund. This would require approval by the Board of Governors by 85 per cent of the total weighted voting power. In addition, every member has the right, under the Articles of Agreement, to "opt out" of a uniform change in par values simply by notifying the Fund within 72 hours that it does not wish the par value of its currency so changed. The United States would make clear in its proposal that not only must the uniform appreciation be approved by the Board of Governors, but that if more than a very small number of countries (say, countries not exceeding 5 per cent of the Fund quotas and excluding any industrial countries) were to "opt out," the United States would not be prepared to proceed with the second half of its proposal. After the 72 hours within which countries can "opt out" had passed following adoption of the uniform appreciation by the Board of Governors, without more than a very few defections via "opting out," the United States would then propose an individual change in the par value of the dollar constituting a depreciation back to where the dollar price of gold would be $35. Once this was approved by the Fund and placed in force, the result would be a major realignment of exchange rates which could be called either an appreciation of other rates relative to the dollar or a depreciation of the dollar relative to other currencies, depending on one's taste and one's national affiliation. One of the major features of this scenario, however, would be that the "burden of initiative" would largely fall on and be taken by the United States. It is clear, of course, that the United States would have to place substantial pressure on other countries to make them "stand still" for the exchange rate change contemplated.

C. The broad rationale for the exchange rate realignment which would be aimed at by this scenario would be essentially as follows:

1. It should be agreed internationally that for a sustained period of time--say, five years as a minimum--the United States and the world should aim for a U.S. official settlements <u>surplus</u> (excluding SDR allocations) in the range of $2-3 billion per year, abstracting from short-term deviations.

2. This should be aimed at by an immediate major realignment of exchange rates, and any individual exchange rate changes proposed by other countries later during the quinquennium should be judged importantly against this generally-agreed objective (see point D below). Adding up the "underlying"

U.S. deficit (i.e., abstracting from existing cyclical and random factors in the present deficit) together with the balance of payments cost of completely liberalizing capital flows and other transactions as well as allowing for an average surplus of $2.5 billion per year (excluding SDR allocations), this would probably mean the need for an annual improvement in our balance of payments on the order of $6-8 billion. It is this range of figures at which a realignment of exchange rates should be targeted. ?

3. The present rate of SDR allocations is undoubtedly too small. In addition, it is based on the assumption that net additions to world reserves in the form of U.S. dollars will be $0.5-1.0 billion, rates which are presently being greatly exceeded and which are likely to be exceeded for the whole of the first three-year period. If the figure of +1.0 billion for reserves created via the U.S. balance of payments (the top of the range in the assumptions stated in the Managing Director's proposal) were replaced by -2.5 billion, the present allocation rate of $3.0 billion annually would have to be boosted to $6.5 billion to produce the same aggregate results in terms of world reserves as was being aimed for. In the context of an agreed exchange rate policy aimed at producing a sustained U.S. official settlements surplus (excluding SDR allocations) of $2-3 billion per year, other countries would necessarily be much more vulnerable to balance of payments difficulty, and might well be willing to support a still higher rate of SDR allocation. Even at an allocation rate of $6.5 billion, however, the United States would receive around $1.5 billion per year, so that in this situation our net reserve position would be improving by around $4 billion per year, or $20 billion over a five-year period.

4. Our willingness and wish to aim for such a surplus would represent, by comparison with the situation today, the provision of substantial additional resources to the rest of the world--something in the neighborhood of 2/3 to 3/4 of one per cent of our GNP and roughly half that proportion of world GNP. For the rest of the world, that would represent not inconsiderable help in dealing with the inflation that nearly all of their Governors complained about at Copenhagen. For us, it would involve somewhat more of an export-led upturn, and the price changes involved (in the form of an exchange rate realignment) could assist materially in resisting domestic protectionist pressures. It is only fair to note, however, that this shift in the use of

resources to the external sector would of course imply the use of correspondingly smaller volume of resources domestically within the United States, and this in turn (both to facilitate the contemplated shift in use of resources and to compensate for its impact on the domestic situation) would imply an additional degree of restraint in fiscal and monetary policies. or less ease

5. We could say that only in connection with such a sustained period of official settlement surplus would we be willing to look seriously at a negotiation contemplating putting the world, including the United States, on a full reserve asset settlement basis. In other words, we might be willing to try to work ourselves out of the reserve currency business--always abstracting from reasonable working balances--but other countries would have to be prepared to accept the implications of this in terms of the exchange rate pattern and balance of payments situations being aimed at.

6. An indirect SDR-aid link, but one of quite substantial quantitative importance, would also be involved in this procedure. The LDC's would receive about one-fourth of any increase in SDR allocations resulting from the proposed shift in the U.S. position. If the assumption is made that their absolute reserve targets (whether implicit or explicit) would not change, the additional SDR allocations would, in effect, be the same as an equivalent amount of completely untied program aid. If the figures given above have some validity, the additional SDR allocations to the LDC's could be in the range of some $950 million per year, an amount of no mean importance when compared with IDA plans and with the external resources otherwise available to the LDC's.

D. The initial result of successfully implementing this scenario would be a large and essentially uniform alteration in the exchange relationship of the dollar to other currencies. It seems fairly clear that at least some currencies, and perhaps quite a few (in terms of numbers of countries) would want to depreciate from the level at which they had been placed at least part way with the dollar and in a number of cases all the way. Such subsequent individual exchange rate depreciations should be dealt with separately in the ensuing period. As a general proposition, the substantive justification for any individual depreciation of this type should be required to show that the country's balance of payments loss from the initial exchange realignment could be expected to exceed its reserve gain from the increased SDR allocations discussed in point C above. In this connection, one might wish to accelerate or "front load" the newly-enlarged SDR allocation process, so as to have the larger amounts available in dealing with initial capital flows stemming from the realignment procedure.

E. One important and obvious question would be the role of gold in the new situation. I have examined carefully over quite a period of time whether there is some procedure--even a quite complex one--by which officially-held gold could be turned in to the Fund, directly or indirectly against SDR's. I have not been able to discover any technique available under the present Articles of Agreement which would accomplish this to any significant degree; it would require an amendment which would necessarily be time-consuming, at the least, to negotiate and get ratified. It is difficult to know what would be likely to happen to the market price for gold after the above scenario had been worked out. The scenario, if it worked, would have the symbolic virtue of showing that, at least for an interim period of a few days, the official gold price could be reduced. Also, and much more important, the anticipated strength of the U.S. balance of payments position should have a dampening impact on the dollar gold price in the markets. To the extent this was a very strong effect, we might find the price falling to or below $35, in which case the present arrangement with South Africa would operate to bring a lot of South African gold into the Fund. We would have to examine whether the present South African arrangement should be terminated or modified, which would be justifiable under the provision of the Fund Decision which states the arrangement "shall be subject to review whenever this is requested because of a major change in circumstances." (For further information on available present techniques for dealing with gold, see the attached memorandum.)

F. Point C.5 above mentioned briefly that the United States might want to be willing to consider, in connection with this scenario, the negotiation of something resembling a reserve settlement account as a means of working our way out of the existing situation in which the U.S. dollar is held in large amounts in the reserves of other countries. We would want to consider whether deliberately working our way out of the <u>reserve</u> currency business could be done in such a manner as to leave the dollar in its <u>vehicle</u> currency role, which there is no doubt is essential, and will doubtless continue to be essential, for the functioning of the system. If we concluded that these two roles could in practice be distinguished, we might well want to engage in a negotiation (which would probably be protracted and which would require amendment of the Articles of Agreement) and to so announce at the time our exchange realignment proposals were unveiled. One form such a proposal might take would be to create a third account in the Fund, into which countries could deposit gold and currencies held in their reserves as of a certain (earlier) date, and against which they would receive SDR's. It would be possible, perhaps, for the dollars deposited in such a conversion account to be simply left there in dead storage. The other possibility would be that the United States would amortize them over a certain agreed period of time with SDR's. If this were the procedure, the United States would of course have to run a balance of payments surplus (on official settlements) of the appropriate size and this would have continuing longer range implications for both the world's exchange rate pattern and the rate of SDR allocation. Finally, in order to avoid the tendency for many countries to begin again holding dollars or other currencies in their official reserves, and thus starting the whole cycle once again, it seems to me doubtful that mere international agreement that this should not be done would be likely to get very far as a practical matter in influencing official behavior. If avoiding foreign currency holdings in reserves above levels constituting reasonable working balances on the one hand, or representing the result of swap transactions on the other, were to be an agreed objective, the best way--and perhaps the only way-- to do this would be to raise the interest rate on SDR's to the point where countries would wish to hold SDR's in their reserves in preference to currencies. This idea would seem to imply that SDR interest rates would have to be fairly frequently adjusted so as to be competitive with the relevant interest rates in the appropriate national or international markets.

G. Other than in those cases where exceptions are expressly mentioned above, everything suggested in this note can be accomplished under existing provisions of national or international law. It is obvious that the negotiating problems would be of a truly extraordinary degree of difficulty and complexity; that technical and policy "spinoffs" from the main propositions briefly put forward above could be major; and that--at least in the short term--financial markets everywhere would be in an uproar. The question is: Can a gradual (or fast) disintegration of the free world's economic and financial system be evaded by any less ambitious proposal?

Attachments

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Attachment 1

Congressional Action

"Pursuant to Section 5(b) of the Bretton Woods Agreements Act, as amended, the Congress hereby authorizes the President, the United States Governor of the International Monetary Fund, and such other officials as may be delegated by them, to make such proposals and to indicate such agreement or approval on behalf of the United States with respect to changes in the par value of the United States dollar (under Article IV, Section 5 of the Articles of Agreement of the Fund) and with respect to uniform changes in the par values of the currencies of all members (under Article IV, Section 7 of the Articles of Agreement of the Fund), as may be deemed by the President to be in the public interest, provided that at no time shall the par value of the United States dollar be equivalent to an official price of gold in excess of 35 United States dollars per fine troy ounce."

Note: Section 5 of the Bretton Woods Agreements Act states, "Unless Congress by law authorizes such action, neither the President nor any person or agency shall on behalf of the United States... (b) propose or agree to any change in the par value of the United States dollar under Article IV, Section 5, or Article XX, Section 4, of the Articles of Agreement of the Fund, or approve any general (sic) change in par values under Article IV, Section 7;...."

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Attachment 2

Appreciation-Depreciation Percentages

Interim Gold Price ($ per ounce)	Percentage Rate of Uniform Appreciation to Reach Indicated Gold Price 1/	Percentage Rate of Dollar Depreciation to Move from Indicated Gold Price back to $35 2/
34.50	1.45%	1.43%
34.00	2.94%	2.86%
33.50	4.48%	4.29%
33.00	6.06%	5.71%
32.50	7.69%	7.14%
32.00	9.38%	8.57%
31.50	11.11%	10.00%
31.00	12.90%	11.43%
30.50	14.75%	12.86%
30.00	16.67%	14.29%
29.50	18.64%	15.71%
29.00	20.69%	17.14%
28.50	22.81%	18.57%
28.00	25.00%	20.00%

1/ This also equals the percentage increase, in U.S. dollar terms, of the price of an imported item whose price in foreign currency remains unchanged, after completion of both steps in the proposed exchange realignment.

2/ This also equals the percentage reduction, in foreign currency terms, of the price of a U.S. export item whose U.S. dollar price remains unchanged, after completion of both steps in the proposed exchange realignment.

~~SECRET~~

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date August 9, 1971

To Chairman Burns

Subject: Questions on Suspension.

From Robert Solomon

STRICTLY CONFIDENTIAL (FR)

Ralph Bryant has set down the attached list of questions on stage-managing a U.S. suspension of gold sales. We shall try to come up with some answers--or at least some considerations that would help in formulating answers.

More important than stage management, of course, are the questions that relate to the substance of the U.S. position in the lengthy negotiations that would follow a suspension.

R.S.

Attachment.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date August 6, 1971

To Mr. Robert Solomon

From Ralph C. Bryant

Subject: Stage-Management of a U.S. Suspension of Gold Sales and Purchases: A Checklist of Questions

STRICTLY CONFIDENTIAL (FR)

It is possible, as we have known for some time, that a suspension of gold sales and purchases could come to seem desirable or even inevitable. As a contribution to our contingency planning, I have been thinking again about the details of stage-managing such a policy action. The purpose of this note is to collect together some pertinent questions.

1. What would be the least unfavorable climate in which to suspend? How far should U.S. reserve assets be drawn down before such action is taken? (On these questions see our memorandum dated May 10, 1971 (?) entitled "Timing of a U.S. Suspension of Gold Sales and Purchases.")

2. Should gold purchases be suspended as well as sales, and should statements about future policy refer to sales and purchases symmetrically?

3. Should U.S. action and/or statements of intention differentiate gold and SDR, or should they be treated equivalently? For example, would we unequivocally suspend SDR sales and purchases?

4. Following suspension, and pending a longer-run resolution of the crisis, should the United States make any use of its reserve assets? Would there be any net advantage in the United States taking an initiative to make a post-suspension distribution of some of our reserve assets to our "friends?" (For example, suppose gold requests from Belgium, France, the Netherlands, and Switzerland had proximately triggered closing of the window, and that as a sweetener to Germany, Japan, and Canada we offered to distribute to these "non-panicky" creditors \$1-2 billion of our gold and reserve position in the Fund.) What criteria could be used to select countries and amounts in such a distribution? Could we legally draw from the Fund after suspending? Could we get Fund Board approval? How much would post-suspension use of our reserve assets weaken or strengthen the incentives other countries would have to reach a crisis resolution quickly?

STRICTLY CONFIDENTIAL (FR)

5. Should a suspension decision be announced publicly at the time it is taken, or should an attempt be made initially to keep it confidential? How long would it be in the interest of hostile countries to keep it confidential that they had found the gold window closed? A confidential suspension might give governments a little time to act without the pressure of crisis headlines -- for example, to meet in Fund or G-10 for the purpose of agreeing on a schedule for further meetings to bargain out a crisis resolution. In the period following suspension and before the public acknowledgment, what line could the Administration take in replying to pointed press questions? What form should a public announcement take (e.g., Presidential speech, news conference, release of official letter to IMF, communique of Group of Ten)?

6. Following open acknowledgment of suspension, what educational activities could members of the Administration take to set the decision in perspective for the general public (and hence to minimize public pressure for a too-hasty, inappropriate resolution of the crisis).

7. What would the exact legal situation be with respect to the IMF Articles of Agreement? With respect to existing U.S. legislation?

8. Should the U.S. monetary authorities intervene in the New York exchange market -- either to drive the dollar to an appropriately large discount vis-a-vis the currencies of strong surplus currencies, to minimize large daily fluctuations in rates, or both? Are there any legal restrictions in U.S. legislation that would prevent us from accumulating a large amount of foreign currencies?

9. How much of the initiative for convening a conference with other governments should be taken by the United States? Is our post-suspension bargaining position stronger or weaker if we sit on our hands and let other countries take the initiative? Could a policy of temporarily sitting on our hands be viable in the face of domestic political pressure? Should the U.S. bargaining position (our preferred longer-run resolution of the crisis) be made public at the outset, or would there be advantages in keeping back some of our possible concessions (e.g., a willingness to reduce the reserve-currency role of the dollar by participating in a general consolidation of reserve assets)?

STRICTLY CONFIDENTIAL (FR)

10. What should policy be with regard to post-suspension use, by the United States or by other governments, of the Federal Reserve and Treasury swap network? (There is of course also a very important set of questions about use of the swap network in the period of time (days or weeks) immediately _prior_ to suspension action.)

IMP

draft
C. A. Coombs:[redacted]
8/13/71

MEMORANDUM TO CHAIRMAN ~~BYRNES~~ BURNS

From: C. A. Coombs

1. Advocates of closing the gold window seem to be overlooking at least one disastrous consequence of such action. This would be the massive ~~or~~ destruction of international liquidity that would ~~inescoriably~~ inexorably follow. The main reason for such a violent contraction of international liquidity would be the general expectation of foreign financial officials of an early increase in the official price of gold internationally, with or without U.S. concurrence.

2. Quite aside from the freezing of our own gold stock resulting from closure of the window, the following major components of international liquidity both here and abroad would be immediately frozen or immobilized:

(a) SDR's. Most countries would refuse to sell any of their present holdings of SDR's, which carry a categorical gold value guarantee, so long as they face the risk of a major increase in the official gold price, either here or abroad.

(b) Closure of the gold window would pull out the cornerstone of the IMF and immediately paralyze any lending operations by that institution.

(c) The Federal Reserve swap network would be ~~XXXX~~ inoperable.

3. The main problem facing foreign countries following closure of the gold window and a floating rate for the dollar would be to negotiate a monetary block among themselves providing reasonable stability in their exchange rates vis-a-vis one another. Otherwise, trade within the Common Market and with adjoining countries would ~~separate~~ suffer a catastrophic decline. In order to maintain such exchange rate stability among themselves, they would have to devise some mutually acceptable system of settling deficits and surpluses in their trade with one another. Over the past 10 years the Federal Reserve swap network, the ~~international~~ IMF quotas and, more recently, SDR's, have provided the financing for the bulk of such payment ~~in~~ imbalances. ~~XX~~ With these sources of liquidity suddenly destroyed or otherwise immobilized, the ~~common~~ Common

Inconvertible,

Market~~s~~ and other foreign countries involved would have to fall back upon their present holdings of ~~XX~~ gold and dollars. Clearly, none of the foreign central banks involved ~~are concerned~~ would be prepared to accept settlement of ~~their~~ trade surpluses by taking still in more inconvertable ~~convertXXX~~ floating dollars from their trading partners in deficit. In effect, therefore, the only effective means of international settlement among ~~common~~ the Common Market and other foreign countries ~~concerned~~ would be their present gold holdings. These gold holdings ~~XXXXX~~ have risen very substantially over the past decade ~~and~~ but ~~are~~ still provide no where near adequate ~~to provide~~ international liquidity for the foreign countries concerned. Moreover, why should they sell gold among themselves at $35.— when the London ~~f~~ free market price might be at $70.—, and the ~~1968~~ March 1968 agreement no longer valid.

X

4. Therefore, the Common Market ~~countries~~ and other foreign countries concerned would be inexorably ~~inescorably~~ compelled to strengthen their reserve positions by jointly taking the action many of them have long since been asking of us, i.e., to raise the official price of gold from $35 to, say, $70. ~~$70~~.

~~XXXXXXXXXXXcXXX~~

The United States, having closed the gold window, would have taken itself completely ~~our~~ out of such a foreign negotiation and could do nothing to stop it. We would then be confronted with a foreign official, and effective, price of gold ~~looking at~~ of, say, $70 looking ~~at~~ down at our ~~normal~~ nominal $35 dollar price. Just as ~~occurred during~~ in the 1930's, we should have no practical alternative but to accommodate our official price~~s~~ to the foreign official price.

5. The sequence of events sketched out above would, I think, be ~~inescoriably~~ inexorably dictated by the facts of the situation created by a U.S. closure of the gold window. On numerous occasions in the past, ~~some~~ individual central bank officials have predicted to me precisely such a sequence of policy actions abroad.

Q.M.P.

August 13, 1971

STRICTLY CONFIDENTIAL (FR)

U.S. Liabilities to Foreign Official Institutions
(Increases; millions of dollars)

	Total	Switzer-land	Germany	France	United Kingdom	Japan	Other
1970 Year	7,344	254	6,151	808	-444	514	61
1971 Q-1	4,546	110	2,019	354	1,049	1,026	-12
Q-2	5,659	350	707	190	1,628	1,916 1/	868
July 2/	2,200	-80	265	725	365	600	325
August 3/							
2-6	920	418	-342	295	60	373	116
9	750	550	--	45	60	59	36
10	270	155	--	58	--	57	--
11	460	60	--	80	250	60	10
12	1,000	625	39	100	120	65	51
13	950	235	5	320	4/ 170	75	145
Aug. 2-13	4,350	2,043	-298	898	660	689	358

1/ Includes increase of $650 million in liabilities to Bank for International Settlements.
2/ Partly estimated.
3/ Based on reports of market interventions by foreign central banks.
4/ U.K. figures not final; may be intervening in New York market.

2 - H. Klein

For Safire's notes on Camp David meeting, August 13-15, 1971

see Name File, Safire, William

SR, 11/83

DOCUMENT OF INTERNATIONAL MONETARY FUND
AND NOT FOR PUBLIC USE

FOR
AGENDA

SM/71/214

Chm Burns
8/18/71 (Art)

August 16, 1971

To: Members of the Executive Board

From: The Secretary

Subject: United States - Exchange System

The attached memorandum of the staff containing a proposed decision concerning the exchange system of the United States will be taken up at the Executive Board meeting scheduled for 4:30 p.m., today, August 16, 1971.

Att: (1)

Other Distribution:
Department Heads
Division Chiefs

INTERNATIONAL MONETARY FUND

United States of America - Exchange System

Prepared by the Western Hemisphere Department

(In consultation with the Exchange and Trade Relations Department, the Legal Department, the Research Department, and the Treasurer's Department)

Approved by E. Walter Robichek

August 16, 1971

On August 15, 1971, the Managing Director received a letter from the U.S. Secretary of the Treasury notifying the Fund that, effective as of that date, the United States no longer, for the settlement of international transactions, in fact, freely buys and sells gold under the second sentence of Article IV, Section 4(b). The Secretary stated that his letter of August 15, 1971 superseded the letter of May 20, 1949, to the Managing Director from the Secretary of the Treasury and Chairman of the National Advisory Council on International Monetary and Financial Problems. The letter of May 20, 1949 had stated that in connection with the obligations of members of the International Monetary Fund under Article IV, Section 4(b), of the Articles of Agreement of the Fund, the Government of the United States, for the settlement of international transactions, in fact was freely buying and selling gold within the limits prescribed by the Fund under Article IV, Section 2. The United States authorities have announced that the Secretary of the Treasury has "strictly limited further use of U.S. international reserve assets (gold, SDR's, drawings on the IMF, or foreign exchange holdings) to settlement of outstanding obligations and, in cooperation with the IMF, to other situations that may arise in which such use can contribute to international monetary stability and the interests of the United States."

The action described in the letter of the Secretary of the Treasury places the United States in the same position as other members of the Fund which, under Article IV, Section 4(b) first sentence, are required to take appropriate measures in order to ensure that transactions between their currencies and the currencies of other members take place within their territories only at rates within the limits prescribed by Article IV, Section 3. The United States authorities have indicated that they are not taking measures for this purpose in accordance with Article IV, Section 4(b). However, the Secretary's letter states that the United States will continue to collaborate with the Fund to promote exchange stability, to maintain orderly exchange arrangements with other members, and to avoid competitive exchange alterations, as required by Article IV, Section 4(a).

The par value of the United States dollar is 15 5/21 grams of gold 9/10 fine (0.888671 gram of fine gold), which is equivalent to US$35 a fine ounce. This par value of the United States dollar was established with the Fund on December 18, 1946 at the time of the initial determination of par values and became effective on that date. The United States authorities have indicated that the official U.S. dollar price of gold has not been altered by the action referred to above.

The United States has been experiencing balance of payments difficulties of varying intensity over a long period of years. The United States has incurred deficits on an official settlements basis in most years of the 1960s, and in 1970 the deficit on this basis reached a record amount of $9.8 billion. A further large deficit was registered in the first half of 1971. In the first quarter of the year there was a deficit on official settlements basis of $4.7 billion ($5.5 billion on a seasonally adjusted basis). In the second quarter of 1971 it is estimated that the deficit was even larger (data on the second quarter balance of payments are expected to become available this week).

Other indicators of the U.S. balance of payments situation have manifested signs of weakness. The position on current and long-term capital account (the basic balance) has been in deficit in most years of the 1960s, and has been consistently in deficit since 1964. These deficits have persisted notwithstanding the application of restraints on the outflow of capital that have been applied in various forms since the early 1960s. In the last few years the basic deficit has been of the order of $3 billion a year, and there are indications that it may have risen in the first half of 1971.

There has been a sharp deterioration on trade account this year, and over the first six months there was a trade deficit of about $400 million, compared with a surplus of $2.7 billion ($2.1 billion on a balance of payments basis) in 1970. It appears that there were some special factors behind the trade performance in the first half of this year, particularly in the second quarter, but there have been official statements to the effect that the trade balance may well be in deficit over the whole of 1971, implying a trade outturn in the second half of this year that was not expected to differ substantially from that registered in the first half.

Also included in the economic program announced by the United States authorities are tax and expenditure reductions, a freeze on wages, prices, and rents for 90 days, and the imposition of a temporary import surcharge, generally at the rate of 10 per cent on goods which are presently dutiable. The United States Government has provided a preliminary assessment of the effects of the aforementioned measures, and the staff will be examining these measures in the light of developing circumstances.

Proposed Decision

In view of the foregoing, the following decision is proposed for the consideration of the Executive Directors:

1. The United States authorities, in a letter from the Secretary of the Treasury to the Managing Director, have notified the International Monetary Fund "that, with effect August 15, 1971, the United States no longer, for the settlement of international transactions, in fact, freely buys and sells gold under the second sentence of Article IV, Section 4(b). The United States will continue to collaborate with the Fund to promote exchange stability, to maintain orderly exchange arrangements with other members, and to avoid competitive exchange alterations." The United States authorities have also stated that they are not taking measures in order to ensure that transactions between their currencies and the currencies of other members take place within their territory only at rates within the limits prescribed by Article IV, Section 3.

2. The Fund notes the circumstances which have led the United States authorities to take the actions described above. The Fund emphasizes the undertaking of members to collaborate with it to promote exchange stability, to maintain orderly exchange arrangements with other members, and to avoid competitive exchange alterations, and therefore welcomes the intention of the United States authorities to act in accordance with this undertaking.

3. The Fund will remain in close consultation with the authorities of the United States and of the other members with a view to the prompt achievement of a viable structure of exchange rates on the basis of parities established and maintained in accordance with the Articles of Agreement. The Managing Director will take appropriate initiatives to this end.

DOCUMENT OF INTERNATIONAL MONETARY FUND
AND NOT FOR PUBLIC USE

Sct. M.P.

FOR AGENDA

EBD/71/202

August 16, 1971

Chm Burns
act) 8/18/71

To: Members of the Executive Board

From: The Secretary

Subject: United States - Article IV, Section 4(b)

There are attached for the information of Executive Directors copies of a letter of August 15, 1971 from the Secretary of the Treasury of the United States, and of a letter, referred to therein, dated May 20, 1949.

Att: (2)

Other Distribution:
Department Heads
Division Chiefs

THE SECRETARY OF THE TREASURY

Washington 20220

August 15, 1971

Dear Mr. Schweitzer:

This is to notify you that, with effect August 15, 1971, the United States no longer, for the settlement of international transactions, in fact, freely buys and sells gold under the second sentence of Article IV, Section 4(b). The United States will continue to collaborate with the Fund to promote exchange stability, to maintain orderly exchange arrangements with other members, and to avoid competitive exchange alterations. This letter supersedes the letter of May 20, 1949, to the Managing Director from the Secretary of the Treasury and Chairman of the National Advisory Council on International Monetary and Financial Problems.

Sincerely yours,

(/s/ John B. Connally)

Secretary of the Treasury
and
Chairman of the National Advisory Council on
International Monetary and Financial Policies

Mr. Pierre-Paul Schweitzer
Managing Director
International Monetary Fund
19th and H Streets, N.W.
Washington, D. C. 20431

THE SECRETARY OF THE TREASURY
WASHINGTON

May 20, 1949

My dear Mr. Gutt:

In connection with the obligations of members of the International Monetary Fund under Article IV, Section 4(b), of the Articles of Agreement of the Fund, I wish to advise you that the Government of the United States, for the settlement of international transactions, in fact freely buys and sells gold within the limits prescribed by the Fund under Article IV, Section 2. The policy of the United States in this respect has not been changed since prior to the signing and entry into force of the Articles of Agreement.

Very Truly yours,

/s/ John W. Snyder
Secretary of the Treasury and
Chairman,
National Advisory Council on
International Monetary and Financial
Problems.

Mr. Camille Gutt
Managing Director
International Monetary Fund
1818 H Street, N.W.
Washington 6, D. C.

I M P.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date August 17, 1971

To Chairman Burns

From Samuel Pizer

Subject: Estimates of revaluation effects on U. S. trade.

CONFIDENTIAL (FR)

The attached memorandum is based on work done over the past several months attempting to evaluate the effects of specified changes in foreign exchange rates on the U.S. trade balance. Results are presented in summary form, not spelling out a number of crucial assumptions detailed in the underlying work, and not attempting to take into account the full range of international transactions or the further effects of changing either capital controls or U.S. and foreign quotas and trade barriers. Nevertheless, it provides a starting point for thinking about some of the magnitudes and relationship involved in negotiating changes in exchange rates.

While there may be differences of judgment as to the precise arithmetic involved, I believe there is substantial staff agreement that the restoration of equilibrium exchange rates from the U.S. point of view requires some major changes in the exchange rates of industrial countries and quite possibly others. Minor changes will only lead to another crisis fairly soon. Moreover, minor changes will not permit the removal of direct controls.

SP

Attachment.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date August 17, 1971

To Chairman Burns (through Mr. Pizer)

From Helen B. Junz H.B.J.

Subject: Preliminary appraisal of possible magnitudes of "acceptable" exchange rate changes as indicated by their effects on the U.S. trade balance

~~CONFIDENTIAL (FR)~~

This memo sets forth some preliminary estimates of the effect on the U.S. trade balance of certain changes in exchange rates of major foreign countries. Within this limited framework, it is possible to draw some tentative conclusion about the adequacy, or otherwise, of the particular magnitudes of possible changes.

Taking account of differences in cyclical situations among industrial countries, it seems that a viable current account position for the United States this year would have required an improvement of the order of at least $5 - $6 billion. Assuming, relatively arbitrarily, that roughly $4 - $5 billion of such an improvement would have to have come from a higher trade surplus, certain conclusions can be drawn.

Earlier estimates showed that, after an appropriate interval of time of something like twelve months or so,[1/] the de facto exchange rate adjustments made before August this year (i.e., revaluations of 5 per cent each by Germany, Austria and

1/ The initial effect of exchange rate changes is likely to be perverse because short-run elasticities are likely to be very small and because imports may be invoiced in foreign currencies. (To the extent that exports also are invoiced in foreign currencies, this effect is offset.) The second factor is probably of less importance in the U.S. than in other cases.

the Netherlands and by 7 per cent and 3-1/2 per cent, respectively, by Switzerland and Canada) are likely to improve the U.S. trade balance by around $3/4 billion annually. The size of the improvement still needed makes it obvious that action by Japan and Canada alone would be insufficient to bring about anything approaching an equilibrium rate for the U.S. dollar. It is also clear that any further moves by European countries will hinge importantly upon the size of any Japanese adjustment.

A 10 - 15 per cent upward revaluation of the Japanese yen is tentatively estimated to improve the U.S. trade balance by $0.9 - $1-1/4 billion. If the Japanese revaluation could tend towards the upper limit of this range, it might not be inconceivable to achieve a further upward adjustment of the German DM (over and above the 5 per cent average appreciation of the past pre-speculation months) of 5 per cent, which in turn might be accompanied by equal adjustments (i.e., 5 per cent) by the remainder of the present Common Market countries (whether or not this would include an additional adjustment for the Netherlands is left open; the difference would be about $0.1 billion in the U.S. trade balance). These moves by the EEC countries could bring about an additional improvement in the U.S. trade balance of around $1-1/2 billion.

Consequently, added to the exchange rate adjustments between May and August 13, upward revaluations of the currencies of the Common Market countries by 5 per cent and of that of Japan by 15 per cent would improve the U.S. trade balance by $3-1/2 billion. An additional revaluation of the Canadian dollar by about 3 per cent and smaller upward adjustments by some of the remaining G-10 countries would bring the total within the postulated $5 billion or so range. Anything less by these countries would put a great deal more of the adjustment burden on countries with weaker payments positions.

The trade balances of most of these countries, especially those of Japan, Canada and Germany, show a relatively strong underlying upward trend. Revaluation effects on their trade balances, particularly if their major competitors move with them, should be tolerable.

It should be noted that the assumption of exchange rate realignment negotiations within the framework of the G-10 is not meant to preclude upward adjustments by other countries. It is not at all clear that some of the oil countries as well as Australia, and possibly some others, could not afford to have their currencies move up against the U.S. dollar. To the extent that this occurred, the needed degree of revaluation by others would be diminished. However, revaluation by oil countries, particularly, would have greater adverse price effects on the United States than on other industrial countries.

Given the relative weights of the G-10 countries in world trade, the adjustments postulated above would average out to a 2-1/2 per cent devaluation of the U.S. dollar. Based on U.S. import weights the devaluation rate would be 5 per cent.

The figures postulated above give some idea of the order of magnitude of exchange rate changes needed to achieve a $5 - $6 billion improvement in the U.S. current payments balance. They cannot indicate whether adjustments of this order are likely to achieve longer-run equilibrium in the overall U.S. payments position. This depends upon longer-term goals regarding the optimal structure of the U.S. balance of payments. In addition, to the extent that a possible removal of controls on capital and trade flows may alter current account surplus aims, exchange rate changes may need to be greater or smaller. To the extent that import surcharges are expected to be retained, exchange rate changes could be less.

It should be kept in mind that the short-run effect of the import surcharges depends heavily upon whether the public believes them to be temporary or not. If they are assumed to be removed when parities are fixed, their effect depends upon how great people believe existing disparities to be. For example, if the general belief is that the Japanese yen is likely to be adjusted by more than 10 per cent, it is that consideration that will govern the movements in imports rather than the surcharge. Whenever the market expects the foreign exchange rate in question to rise by less than 10 per cent against the dollar, the surcharge would temporarily cut imports; whenever the expectation is for a rise by more than 10 per cent, imports would be temporarily stimulated.

cc: Board Members

Messrs. Holland and Partee
Messrs. Gemmill, Bryant, Sammons, Katz and Mrs. Junz

August 16, 1971 - 71/110

STRICTLY CONFIDENTIAL (FR)

Statement by the Economic Counsellor
at EBM/71/88, August 16, 1971 (afternoon)

As the Managing Director indicated this morning, we have been giving attention for some time to the issues involved in the elaboration of a set of parities that could form the basis for a better balance in international payments. In this exploration our attention has been focused primarily on the industrial countries, which have been the area of the most severe disturbances in international payments in recent years. But in this context we have also given attention to rate changes that might be advisable for the primary producing countries.

Logically, this problem can be seen as having two separate aspects. (1) The determination of exchange rates; and (2) the link between the pattern of exchange rates and gold, which would be determined by the price of gold in terms of one of the currencies in the pattern.

The first aspect--that of exchange rates--determines the relative competitiveness of countries in international transactions and the relative value of reserves held in various currencies. The second aspect determines the value of gold, SDRs, and reserve positions in the Fund in terms of currencies.

While it is logically possible to separate these two aspects, it would seem more likely that agreement could be reached on both aspects if both questions were settled at the same time.

The discussion in the remainder of these remarks is addressed to the question of relative exchange rates only.

A satisfactory new pattern of exchange rates could not be found by letting all currencies float for a certain period. Quite apart from the profound uncertainty that such a situation would create, a regime of many floating currencies cannot even in theory be expected to lead to a viable system of rates. This is so, inter alis, because the floating rates would be too much affected by the extent to which countries practiced controls on capital movements and intervened in the market, as well as by anticipations of official actions.

It will be necessary, therefore, to derive a new pattern of exchange rates on the basis of analysis. The central point is clear, namely, that it will be necessary to bring about a certain degree of depreciation of the U.S. dollar vis-a-vis other currencies in order to strengthen the U.S. basic balance and, in particular, the U.S. current account. In this connection, it has to be borne in mind, as was already pointed out in the Annual Report, that the underlying U.S. current account is substantially

- over -

weaker than the $2.5 billion surplus shown in 1970, because that current account position was the result of a recession in the United States occurring at the same time that high employment situations prevailed in the majority of the other industrial countries.

To create a sufficiently large current account surplus in the U.S. balance of payments will require an adequate average depreciation of the U.S. dollar against other currencies. In the staff's opinion, a decline in the value of the U.S. dollar in terms of other currencies on the average by approximately 10 per cent would be sufficient for this purpose. It would not be appropriate, however, to adjust the rates of the U.S. dollar on all currencies by the same percentage. In order to derive the most suitable pattern of rates, it will be necessary to take into account the actual payments positions of individual countries (with adjustment for cyclical factors), the normal payments position to which it may be assumed that each country is directing its policies, and the extent to which each country would be affected by changes in the rates of exchange for the currencies of all other countries.

The calculations involving all these aspects are necessarily quite complex. Our preliminary findings suggest that the new pattern of rates for the main industrial countries (other than the United States) would involve an increase in the rate of the currency of every one of these countries in terms of the dollar. However, there is a clear distinction between at least two groups of industrial countries. For one of these groups the relative appreciation in terms of the dollar should be less than the approximate average of 10 per cent. For the other group--the strong surplus countries--an appreciation somewhat in excess of 10 per cent would appear appropriate. These measurements take their starting point from the parities prevailing before May 30, 1970.

It may also be useful at this stage to make certain related suggestions applicable to certain other Fund members.

1. It may be expected that countries with very close economic relations with the United States, in the sense that a large proportion of their trade and invisibles are with the United States, would want to keep their exchange rate on the U.S. dollar unchanged.

2. It may similarly be expected that many countries with close economic relations with the United Kingdom and France would want to keep their rates on sterling and the French franc respectively unchanged.

3. Countries that are at present in payments difficulties, wherever situated or whatever reserve center they might be most closely linked to, might use this opportunity to lower the value of their currencies compared to the average of other currencies. For some countries a sufficient average depreciation might be achieved by keeping the rate on the U.S. dollar; for other countries it might be advisable to depreciate beyond this point.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

August 17, 1971

TO: Board of Governors

FROM: Samuel Pizer

STRICTLY CONFIDENTIAL (FR)

The attached statement prepared by Mr. Polak at the IMF was supplied to us by Mr. Dale. I believe it is interesting and important as a reflection of the thinking of the Fund's staff on the extent of the exchange rate adjustment that might be necessary. Of course, it needs to be kept STRICTLY CONFIDENTIAL.

SP

Attachment.

cc: Messrs. Holland and Partee
Officers in the Division of International Finance