583

92d Congress
2d Session } JOINT COMMITTEE PRINT

GOLD, SDR'S, AND CENTRAL BANK SWAPS

REPORT

OF THE

SUBCOMMITTEE ON INTERNATIONAL EXCHANGE AND PAYMENTS

OF THE

JOINT ECONOMIC COMMITTEE CONGRESS OF THE UNITED STATES

TOGETHER WITH

ADDITIONAL VIEWS

NOVEMBER 18, 1972

Printed for the use of the Joint Economic Committee

U.S. GOVERNMENT PRINTING OFFICE
85-782 O WASHINGTON : 1972

For sale by the Superintendent of Documents, U.S. Government Printing Office
Washington, D.C. 20402 - Price 15 cents
Stock Number 5270-01643

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LETTERS OF TRANSMITTAL

NOVEMBER 15, 1972.

To the Members of the Joint Economic Committee:

Transmitted herewith for the use of the members of the Joint Economic Committee and other Members of Congress is a report of the Subcommittee on International Exchange and Payments entitled "Gold, SDR's, and Central Bank Swaps."

The views expressed in this subcommittee report do not necessarily represent the views of other members of the committee who have not participated in the hearings of the subcommittee or in the drafting of this report.

Sincerely,

WILLIAM PROXMIRE,
Chairman, Joint Economic Committee.

NOVEMBER 13, 1972.

Hon. WILLIAM PROXMIRE,
Chairman, Joint Economic Committee,
Congress of the United States,
Washington, D.C.

DEAR MR. CHAIRMAN: Transmitted herewith is a report of the Subcommittee on International Exchange and Payments entitled "Gold, SDR's, and Central Bank Swaps" together with additional views by Senator Javits. Representative Boggs was missing in Alaska at the time this report was under consideration. The report has the endorsement of all other members of the subcommittee.

The subcommittee wishes to express its appreciation for the guidance it has received from the administration officials and the private experts who appeared before it as witnesses during the hearings which preceded this report.

Sincerely,

HENRY S. REUSS,
Chairman, Subcommittee on International Exchange and Payments.

GOLD, SDR'S, AND CENTRAL BANK SWAPS

During the week of September 11, 1972, the Subcommittee on International Exchange and Payments conducted 3 days of hearings to review U.S. policies regarding (I) continued reliance upon gold as reserve asset, (II) the future of special drawing rights (SDR's), and (III) the use of the central bank swap network to defend exchange rates. The subcommittee did not investigate the full range of issues that must be resolved among the members of the International Monetary Fund (IMF) before an agreed monetary reform can be implemented. Instead, we were interested primarily in interim measures that would help reinforce the Smithsonian Agreement, announced December 18, 1971, and preserve the multilateral operation of the international payments system. Some of our suggested interim measures do, however, carry implications for long-term reform.

Monetary reform will take at least a year and probably longer to negotiate. During this interim, it is important that the payments mechanism among IMF members function as smoothly as possible and that the introduction of any new payments restrictions be kept to an absolute minimum. These objectives are worth while in themselves as a means of encouraging continued expansion in international trade and of facilitating a recovery in the U.S. balance of payments. In addition, the type of reform that is ultimately negotiated will be influenced by events during the period of transition that began on August 15, 1971, and will end only when a reworked system is finally implemented. To the extent that the United States is cooperative, helps preserve a multilateral payments system, and acts to minimize any disturbances that occur during the period of negotiations, reform will probably be agreed upon more quickly, and other countries also will tend to be less adamant about their own positions.

THE FOCUS OF THE HEARINGS

Gold has long tended to be a stumbling block among the industrial countries whenever they have attempted to devise a common solution to international monetary problems. The French have frequently championed those interests that desired to preserve or even expand gold's international monetary role. By contrast, the United States has through both dollar-financed deficits and announced policies sought to diminish the role of gold as a reserve asset. As the following recommendations demonstrate, action can be taken even before a comprehensive monetary reform is negotiated to remove gold from the area of contention. These initiatives would at the same time pave the way for ultimately phasing out gold as a reserve asset and substituting an internationally created and managed asset, such as special drawing rights (SDR's), in its stead.

In August the Federal Reserve System resumed use of the currency swap network among central banks for the purpose of intervening

in the foreign exchange market to support the dollar. This was the first time the United States had drawn upon the swap network since before the introduction of the new economic policy about a year earlier. While the Federal Reserve intervention was small, it was well timed and widely hailed as an indication that the United States cared about preserving the Smithsonian Agreement and the multilateral payments system. The subcommittee, however, was concerned that currency swaps might once again, as in August 1971, become a vehicle for maintaining an overvalued dollar exchange rate. In the course of the hearings, Under Secretary of the Treasury Volcker and Chairman Burns of the Federal Reserve Board both assured us that, to the best of their abilities, they would ensure that the United States would not again intervene directly or indirectly in exchange markets to support the dollar in the face of an enduring disequilibrium.

I. Deemphasizing Gold as a Reserve Asset

The functions of gold in the international monetary system have been very substantially circumscribed since 1960. After a rush by foreign central banks to exchange dollars for gold in late 1960, the monetary authorities of seven major industrial countries formed the London Gold Pool the following year to help conserve existing monetary gold stocks. When private demand for gold in the London market was high, the pool supplied enough of the metal to keep the price near the then $35 per ounce official level. When there was an ample supply of gold in the London market, the pool purchased. This arrangement worked satisfactorily until early 1968, when private speculative demand for gold became almost insatiable and the members of the pool were called upon to supply more gold than they were willing to relinquish. As the major participant in the pooling arrangement, these losses of gold reserves fell most heavily upon the United States.

In March, 1968, therefore, the members of the pool gathered in Washington and agreed to suspend operations. A two-tier gold market was established. In the free market, private purchasers and sellers meet and exchange gold at whatever price happens to be dictated by the convergence of supply and demand. In the other, official monetary institutions continued to exchange gold among themselves in balance-of-payments settlements at the official value of $35 per ounce. The United States continued to maintain the convertibility of foreign officially held dollars into gold. The pool members also agreed not to buy gold directly from South Africa or on the free market and not to sell it to private parties.

Some European nations, however, wanted South African gold to continue entering the international monetary system. This position was opposed by the United States. After over a year and a half of wrangling about how the output of South African mines would be handled, a compromise was reached under which the International Monetary Fund agreed to buy gold from South Africa whenever the price fell below the $35 per ounce official level or whenever South Africa had a payments deficit. Under this agreement, the IMF purchased $640 million worth of South African gold in 1970 and $138 million worth last year. None, however, has been purchased by the Fund since August, 1971.

For about the last year, South Africa's balance of payments has been strong, and gold prices in the free market have remained above the official level. Consequently, South Africa has not been able to meet the criterion for gold sales to the International Monetary Fund. Moreover, the amount of gold it has supplied to the private market has been reduced, since South Africa has not needed to sell its full output in order to meet payments to foreigners. Both the reduction in supply and increasing speculative demand have contributed to pushing the free market price to around $70 an ounce, or nearly double the official value of $38 per ounce. For a few weeks, the private market price of gold fluctuated between $65 and $70 an ounce, but the price has now dropped.

The high private market price of gold has tended to strain the monetary arrangements devised at the Smithsonian. Soaring gold prices place the exchange value of the dollar under suspicion. Moreover, the high private market price of gold has made official monetary institutions reluctant to use the metal in settling balance-of-payments deficits. Because the value of special drawing rights is also defined in gold, a similar reluctance to use SDR's has emerged. While the proportion of gold in total international monetary reserves has declined from 70 percent in 1950 to 50 percent in 1970, and now stands below 30 percent, it is not a healthy development to have a significant portion of the world's monetary reserve assets immobilized.

Before August 15, 1971, when the United States continued to maintain convertibility into gold of foreign officially held dollars, it made sense to prohibit central banks from selling gold in the private market. Otherwise, these institutions would have been able to obtain gold from the United States at $35 per ounce and then sell it at a higher price to private purchasers, thus causing a drain of U.S. monetary gold. Now, however, the rationale for prohibiting sales of gold in the private market by the monetary authorities no longer exists.

***Recommendation 1.* The March 1968 two-tier gold agreement should be modified to permit, at their own initiative and volition, sales of gold in the free market by the International Monetary Fund and central banks. On the other hand, the prohibition against central bank purchases of gold in the free market or directly from South Africa ought to be maintained.**

The March 1968 agreement is embodied only in a communique issued by the representatives of the former Gold Pool countries. This arrangement could be easily modified by the group of the 10 major industrial nations or by the Executive Directors of the IMF. Sales of gold in the free market by the International Monetary Fund or by central banks at their own volition would have a number of beneficial effects.

First, such sales would reduce the free market price and therefore help ease the apprehensions that currently exist about the viability of the Smithsonian monetary arrangements. In addition, a lower free market price would make monetary authorities less reluctant to use their remaining gold reserves and their SDR's in international settlements.

Second, sales by central banks—without purchases—would decrease the global stock of monetary gold reserves. A gradual decline in the stock of gold reserves is consistent with and would help advance the longrun U.S. objective of phasing gold out as a monetary reserve asset.

Third, official sales would demonstrate that gold has no immutable intrinsic value. The private price of gold is based on a limited number of transactions in an extremely thin market. This market is protected by the umbrella of the March 1968 two-tier agreement and the December 1969 IMF-South African accord. From 1934 into the 1960's, it was the United States which guaranteed the value of gold. More recently this duty has been shared cooperatively among several industrial nations. It is time, now that we have special drawing rights created by the IMF, to begin withdrawing the mantle of official protection over gold.

Fourth, as the largest official gold holder in the world, the United States would profit from a share of the sales in the private market. At the end of July, the United States had $10.5 billion worth of gold, Germany held $4.4 billion worth, Franch $3.8 billion, Switzerland $3.2 billion, Italy $3.1 billion, the Netherlands $2.1 billion, and Belgium $1.7 billion. All other nations, including Canada and Japan, held less than a billion dollars worth of gold.

Currently the IMF Articles require 25 percent of quota subscription payments to the Fund to be made in gold. Thus, whenever a new member joins the Fund, it must obtain by some means a sufficient quantity of gold to pay one-quarter of its quota in this fashion. The remaining 75 percent is paid in its own national currency. An even more intense scramble for gold occurs whenever the quotas of all IMF members are reviewed, and an across-the-board increase is introduced. The resultant swaps and loans of gold among the Fund and its members to meet the letter of the articles is a testament to the financial imagination of that institution, but little else. In addition, if a member holding gold in its reserve stock borrows from the IMF, repayment of this loan must be made in gold according to the relative proportion of that metal in the country's total reserve holdings.

Ultimately special drawing rights should become the backbone of the international monetary system, and the supply of reserves should be determined jointly by the membership of the International Monetary Fund. Consequently, the role of SDR's should be accentuated whenever possible and gold should be gradually de-emphasized.

Recommendation 2. **Under a reformed international monetary regime, special drawing rights should be made acceptable in lieu of gold in all transactions between the IMF and its member countries.**

Once SDR's become the chief international reserve asset, the path will be open to removing the mystique from gold and making it a commodity like silver, tin, copper, or platinum. Just like any other commodity, the value of gold should be determined by the economics of mining and refining it, on the one hand, and by demand for industrial and artistic uses and for investment as a personal store of wealth, on the other. A major step in this direction will have been achieved when private American citizens are free once again to buy, sell, and hold gold at their own discretion.

In discussing repeal of the present statutory prohibition against private ownership of gold by U.S. citizens, Under Secretary Volcker testified, "The time for sympathetic consideration to the elimination of our own restrictions is when the shape of the new monetary structure emerges, and the monetary system is fully insulated from instability in private gold markets." One could argue that the international monetary system is already largely insulated from events in the private gold market. Indeed, a very substantial rise in the free market price of gold has not impaired international trade or contributed substantially to restrictions on capital flows. The ability of the system to continue functioning despite large fluctuations in the private price of gold is evidence of a degree of insulation. Nevertheless, once an international monetary reform has been negotiated and put into effect, the system will undoubtedly be even more effectively protected from fluctuations in private speculative demand for gold and variations in the amount supplied by South Africa and the Soviet Union. Once the coming reform has been achieved, therefore, there should be no further reason to deny American citizens the same privilege that is enjoyed by private individuals in many other countries.

Recommendation 3. **As soon as the international monetary reform that is currently being negotiated is achieved, all prohibitions on the purchase, sale, and holding of gold by American citizens should be promptly abolished.**

Both occasional sales of gold by monetary authorities in the free market and the abolition of the statutory prohibition against ownership of gold by private Americans would be steps toward removing the mystique from gold and making it a commodity that is traded in the same manner as other metals.

A third factor contributing to the unique status of gold is the December 1969 agreement with South Africa under which the International Monetary Fund agreed to purchase gold from that country under specified circumstances. The March 1968 two-tier marketing agreement, as it is currently being applied, and the December 1969 arrangements between the IMF and South Africa together insure that the price will not fall below $35 per ounce.

At the moment any such prospect seems fanciful. However, given sales by monetary authorities, dishoarding by Europeans, Middle Eastern sheiks, and Indians—all combined with the absence of any commitment by the IMF to buy South African gold—the price could fall to a level unknown since before 1934. On the other hand, permitting Americans to hold and deal in gold would tend to have the opposite impact.

But there would be no need under an SDR-based monetary system to be concerned about whatever the free market price of gold happened to be. If some nations wished to retain some gold reserves and have these assets appraised at their official value, such a desire should create no special problems. The supply of reserves would be governed by the rate of distribution of special drawing rights, and balance-of-payments surpluses and deficits would be settled either in SDR's or in assets, such as gold or foreign exchange, whose value would be determined by their relationship to special drawing rights. The preservation of international monetary stability does not oblige either the United States

or the International Monetary Fund to saddle itself with the responsibility of guaranteeing a market for South Africa's chief export commodity. The purchasing agreement with South Africa, therefore, ought to be allowed to expire naturally in December 1974.

***Recommendation 4.* The current agreement committing the International Monetary Fund to purchase gold from South Africa under certain conditions ought not to be renewed. Instead, it should be terminated in 2 years when it expires.**

II. Strengthening the Special Drawing Rights Mechanism

When the special drawing rights mechanism was added to the IMF Articles of Agreement, the drafters envisioned that decisions would be made to distribute SDR's every 5 years. Instead, the initial agreement was to allocate 9.3 billion of SDR's over a 3-year period. The last of the agreed distributions was made on January 1, 1972. Consequently, a decision must be reached shortly on whether to continue creation and allocation of special drawing rights or to permit the facility to fall into disuse for at least an interim period.

Cogent arguments can be made to the effect that, because there is currently an excess of international liquidity resulting from the almost $30 billion U.S. official settlements deficit in 1971, no more SDR's should be distributed at this time. A break in the distribution of special drawing rights, the exponents of this position might argue, would tend to increase their scarcity value and make them even more desirable as reserves. The most recent problem regarding SDR's, however, has been an unwillingness on the part of holders to use them because their value is defined in terms of gold. High free market prices for gold have made monetary authorities reluctant to use not only that metal as payment for external deficits, but special drawing rights as well. With the issuance of further SDR's, their actual use—which is the important criterion—should increase at least marginally.

On the other hand, any additional issue of SDR's for the 2 years remaining in the current "basic period" should probably be of nominal proportions. If the U.S. balance of payments strengthens markedly, this development would make monetary authorities more willing than they currently are to hold dollars as reserves. Currently many monetary authorities are unwilling holders of excessive dollar reserve balances. The development of a U.S. payments surplus would improve the quality of these balances and, by prompting central banks to hold willingly larger quantities of dollars, would probably increase the net amount of reserves that are available to finance payments imbalances. By contrast, if the United States continues to run official settlements deficits, foreign official dollar balances will expand further. Both the reluctance on the part of surplus nations to accept dollars, and the unwillingness of deficit countries to relinquish gold and SDR's, will grow. In either case, it is difficult to maintain that a large issue of special drawing rights would either promote international monetary stability or substantially enhance the long term viability of the SDR mechanism. Whatever distribution is agreed upon, therefore, should be limited in amount.

***Recommendation 5.* To prevent the International Monetary Fund's special drawing right facility from falling into disuse, the members of the IMF should promptly agree to distribute a reasonable amount of SDR's in 1973 and 1974.**

The amendment to the Articles of Agreement empowering the International Monetary Fund to create and distribute special drawing rights incorporated a compromise specifying that SDR's would be allocated according to each nation's quota in the IMF. A country's quota signifies how much in gold and its own currency that particular nation has contributed to the assets of the IMF. The size of individual member's quotas is determined by their GNP, population, value of international transactions relatives to GNP, and several other factors.

But the decision to distribute SDR's in proportion to quotas was a purely political compromise. It has no economic rationale and, in fact, flies in the face of equity. The outcome of this compromise has been to give most of these assets created by the Fund to the industrial giants of the world—those nations with the highest per capita incomes. Sixty-three percent of the SDR's created have been allocated to industrial countries, 9 percent to other less wealthy developed nations, and only 28 percent to developing countries.

Because of the obvious inequity engendered by allocation of most of the IMF's new international money to the wealthiest nations of the world, the SDR distribution mechanism has been under attack almost since its inception. Suggestions have been made to modify the allocation arrangements and make them more equitable. Two of the options, for example, are either to increase the quotas of the developing countries directly or to allocate some portion of SDR distributions to the International Development Association (IDA) the soft-loan affiliate of the World Bank.

The less developed countries have unified behind a demand for modification of the SDR distribution mechanism in any reformed international monetary system. If these nations stick together, they have sufficient votes to block any amendment of the IMF Articles of Agreement that would be necessary to implement an agreed reform proposal. Fortunately, several of the industrial countries—but not yet the United States—have now altered their positions to favor a change in the SDR distribution mechanism that would give developing countries a larger share than they currently receive.

A change in the pattern of SDR distributions would have a minimal impact on the international monetary system. Since the developing countries would undoubtedly spend most of their additional special drawing rights for increased imports or use them to service existing debts to industrial-country creditors, the SDR's would still eventually end up in the possession of central banks in industrial nations. Opponents have argued that increasing the proportion of SDR's allocated to developing countries would tend to lead to excessively large global distributions. But under the existing SDR amendment, 85 percent of the voters in the Fund must be in favor of a suggested distribution if it is to be approved. With a 15 percent negative vote able to block distribution, any significant reservations should certainly be able to prevent IMF profligacy.

The Joint Economic Committee has long been interested in the potential for using reserve creation by the International Monetary

Fund to finance an increased transfer of real resources from industrial to developing countries. The initial position of this subcommittee, in 1965, was to maintain independent and separate mechanisms for creating reserves and providing development assistance.[1] However, after consideration of a report submitted later in 1965, by Representatives Henry S. Reuss and Robert F. Ellsworth,[2] a study by staff economist John R. Karlik published in April, 1969,[3] and testimony received in hearings during May, 1969,[4] the subcommittee reversed its position and submitted a report proposing to link reserve creation and development assistance.[5] While there are disadvantages to a link, further analysis had indicated that the drawbacks could be curtailed and would be outweighed by the benefits from increasing the flow of financial assistance to poor nations. The essence of the August, 1968, report was endorsed by the majority of the Joint Economic Committee in its annual report issued in March, 1970.[6] The same point of view was expressed by the full committee in a bipartisan analysis of international economic issues contained in the 1971 annual report,[7] and was again confirmed by the majority in the 1972 report.[8]

Another problem that must be resolved as a part of a comprehensive international monetary reform is how to dispose of the excess dollar balances that foreign central banks have accumulated as the consequence of U.S. payments deficits and now hold involuntarily. The most frequently offered suggestion would entail an exchange of official dollar assets in excess of working balance requirements for a special issue of SDR's. It is likely that the interest rate paid on special drawing rights will be increased in the process of monetary reform to make these assets more attractive to official holders. Nevertheless, the possibility exists that the International Monetary Fund may earn more on the dollar assets turned in to it by national monetary authorities than it pays on the special issue of SDR's distributed in exchange. Such net profits, if they indeed accrue to the Fund, could also be channeled to IDA for the benefit of developing countries.

***Recommendation 6.* In the process of reforming the international monetary system, the SDR distribution formula should be revised to assure that a larger proportion of these assets than in the past will be allocated, directly or through international institutions, to developing countries. Also, if the exchange of excessive outstanding dollar reserves for a special issue of SDR's causes net profits to accrue to the International Monetary Fund, these profits should also be used to increase financial assistance to developing countries.**

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[1] Subcommittee on International Exchange and Payments, Joint Economic Committee, U.S. Congress, *Guidelines for Improving the International Monetary System*, Report, August 30, 1965, pp. 11–12.

[2] Representative Henry S. Reuss and Robert F. Ellsworth, *Off Dead Center: Some Proposals to Strengthen Free World Economic Cooperation*, A Report to the Joint Economic Committee, U.S. Congress, December 20, 1965, pp. 14–17.

[3] John R. Karlik, *On Linking Reserve Creation and Development Assistance*, A Staff Study prepared for Use of the Subcommittee on International Exchange and Payments of the Joint Economic Committee, U.S. Congress, April 14, 1969.

[4] Subcommittee on International Exchange and Payments, Joint Economic Committee, U.S. Congress, *Linking Reserve Creation and Development Assistance*, Hearing, May 28, 1969.

[5] Subcommittee on International Exchange and Payments, Joint Economic Committee, U.S. Congress, *A Proposal to Link Reserve Creation and Development Assistance*, Report, August 15, 1969.

[6] Joint Economic Committee, U.S. Congress, *1970 Joint Economic Report*, pp. 52–53.

[7] Joint Economic Committee, U.S. Congress, *1971 Joint Economic Report*, pp. 13–15.

[8] Joint Economic Committee, U.S. Congress, *1972 Joint Economic Report*, pp. 65–66.

III. The Use of Currency Swaps To Finance Central Bank Intervention in Exchange Markets

In 1962 the Federal Reserve System and several foreign central banks established an arrangement under which they agreed to exchange, or swap, equivalent amounts of their currencies when such transactions would be useful in smoothing what would otherwise be large fluctuations in exchange rates. Swaps have usually been arranged between the central banks of strong and weak currency countries. The monetary institution responsible for defending a currency under attack would generally initiate the swap and then use the foreign currency so obtained to buy its own money in the exchange market. Swaps have usually been negotiated when private speculators, because of balance-of-payments trends or political developments, have anticipated an exchange rate change and therefore have moved short term assets across national boundaries so as to profit from the expected devaluation or upward revaluation. When monetary authorities have disagreed with the private speculators' analysis for the need for an exchange rate change, then the officials would generally use the swap network to counter the effects in exchange markets of capital flows.

On June 30, 1971, the Federal Reserve System's net drawings under swap arrangements amounted to $650 million. By the close of business on Friday, August 13, this amount had increased to over $3 billion. Most of this increase, amounting to nearly $2.4 billion, occurred during the week of August 8 to 13.

During August, 1971, the United States was an essentially passive participant in decisions to use the swap network. As the dollar came under attack, foreign central banks purchased these dollars with their own currencies. They did so to prevent the dollar value of their own currencies from breaking through the 1 percent ceiling above parity that was then specified by the IMF. As these foreign monetary authorities accumulated dollars, they requested an exchange rate guarantee against the risk they were assuming. The alternative would have been to insist upon exchanging these dollars for gold. In effect, the Federal Reserve agreed to exchange dollars that were not covered by any guarantee for others that were. When swap lines became exhausted, foreign authorities were offered instead Treasury securities bearing a similar guarantee.

The availability of the swap mechanism and Treasury securities incorporating maintenance-of-value clauses tended to postpone confrontation of the basic reality that the dollar was overvalued and that existing exchange rates could not be maintained. As a result of the exchange rate realignment that was finally negotiated, the Federal Reserve and the Treasury together will be required to ante up a total of approximately $330 million to meet the cost of the guarantees they had extended. This amount—while hardly insignificant—is less important than the consequences of postponing exchange rate realignment in terms of expanding imports into the United States, depressing our exports, and encouraging investment abroad.

In their testimony, both Under Secretary Volcker and Chairman Burns assured the committee that, to the best of the capabilities of their respective institutions, the swap mechanism would never again be used to prop up an overvalued dollar exchange rate or delay a necessary exchange rate adjustment.

Under Secretary Volcker said in his testimony presented September 11, 1972 (pp. 7–8 of his prepared statement):

> We have not embarked on any efforts to artificially prop up the dollar counter to any basic balance-of-payments trends in the longer run. . . . In contrast to usual practices before August 15, . . . the basic initiative will lie with the United States. Foreign exchange will be drawn not in a passive manner after intervention by other countries, but for use in the exchange markets by the United States in such amounts and at such times as we believe the market impact will be favorable and help to curb unwarranted speculative forces. . . . Drawings would not be made or enlarged to deal with what would be fundamental misalinements in our own payments position. In normal and forseeable circumstances, repayment could be anticipated from a reversal of market flows.

Similarly, when Chairman Burns appeared before the subcommittee on September 15, 1972, he said (p. 8 of his written statement):

> In the new operations, market intervention will be on the Federal Reserve's initiative. It will be undertaken only to prevent or counteract disorderly market conditions and will be in such amounts and at such times as are judged likely to have a favorable impact. Swap drawings will not be made for the purpose of providing medium- or longer-term financing of the U.S. payments deficit. Nor will they be used as a substitute for needed adjustments in basic economic policies.

***Recommendation 7.* The swap network among central banks should be used to finance only temporary payments outflows that can be expected to reverse themselves in a matter of months. Exchange market intervention financed through either the swap mechanism or Treasury obligations bearing an exchange rate guarantee should never again be used to postpone an exchange rate adjustment necessitated by fundamental balance-of-payment trends.**

ADDITIONAL VIEWS OF SENATOR JAVITS

The Report of the Subcommittee on International Exchange and Payments is most valuable and should be an important contribution to the ongoing debate. I would be remiss, however, if I failed to point out that this valuable Report does not mention the welcomed U.S. initiative by President Nixon and Treasury Secretary Shultz at the recently concluded IMF–IBRD Annual meeting. At this meeting the United States clearly signaled to the world its willingness to take a leadership role in the upcoming reform of the international monetary system. The recent communique released after the Common Market Summit meeting, in turn, contributes to the forward movement toward the long term reform of the international monetary system. The outward looking nature of this communique which was reinforced by the statements of Western European leaders gives encouragement to those of us who favor an open international trading and monetary system as contrasted with restrictive, inward-looking trading and/or monetary blocs.

Concerning the specifics of the report, I do not feel that it is realistic to expect that "action can be taken even before a comprehensive monetary reform is negotiated to remove gold from the area of contention." But, I do support the concept that gold should be relegated to the status of other commodities over a suitable transition period, and that the importance of SDR's within the international monetary system should be significantly strengthened.

I strongly welcome the emphasis given in the report to using future reserve creation by the International Monetary Fund to finance an increased transfer of real resources from industrial to developing countries.

This "link" is clearly the means for integrating the developing world into the mainstream of trade and commerce, and for the long term opening up of vital new markets for industrial goods. It is my prediction that if this integration does not take place at an accelerated pace over the short term, that the industrialized world will have jeopardized its own future prosperity and well-being.

Better income distribution within societies leads to stronger societies and more sustained economic growth, as the United States and Western European examples make clear. Similarly, better income distribution among societies through the means of future SDR creation through the mechanism of the "link" will lead to a stronger world trading and monetary system, accelerated world economic growth, and reduced tensions among nations.

Therefore, while I welcomed the emphasis given in the Common Market Summit Communique to the problems of the less developed world, I regret that the communique did not mention the "link."

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