



BOARD OF GOVERNORS  
OF THE  
FEDERAL RESERVE SYSTEM  
WASHINGTON

OFFICE OF THE CHAIRMAN

March 1, 1962

The Honorable Robert S. Kerr,  
United States Senate,  
Washington 25, D. C.

Dear Senator Kerr:

In your letter of February 17, 1962 you asked six questions in connection with the proposed foreign exchange operations of the Federal Reserve System.

The answers to these questions are given as follows:

Q.1. Has this proposal been implemented or is it about to be implemented?

- (a) If the answer is "yes," then to what extent in terms of dollars would be invested in foreign currencies?
- (b) For what period of time is it contemplated that this new program will continue?

A.1. The Federal Reserve has recently acquired small amounts of several convertible currencies widely used in international transactions from the Treasury Stabilization Fund and has opened accounts with several European reserve banks. We expect to acquire further amounts through open market purchases of cable transfers or bills of exchange, at home or abroad, when conditions on foreign exchange markets are favorable. From time to time, we may also acquire holdings of foreign currencies through reciprocal transactions with foreign reserve banks. One such transaction with the Bank of France was announced today. (See attached press release.)

The amount of dollars to be invested in foreign currencies will depend upon the needs encountered in specific situations. The Federal Reserve will publish its aggregate holdings of foreign currencies monthly in the Federal Reserve Bulletin. The Federal Reserve will not, of course, be in a position to reveal foreign currency operations before or pending their execution nor the amounts involved in planned or pending operations.

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The period for which the program will continue also will depend upon need and experience. If a need is demonstrated and the program proves useful, it may be continued indefinitely. Otherwise, it will be abandoned.

Q.2. Would the dollars used in the purchasing of the foreign currencies contemplated become additional claims against our gold reserve?

A.2. There is indeed a risk that additional dollars put into the hands of foreigners through our foreign exchange purchases might, at least in theory, become a claim against our gold reserve. In practice, however, the likelihood of this risk materializing would be small, even remote.

We could always resell the foreign currency acquired and thus remove the dollars sold to foreigners from their holdings, in this way eliminating them as potential claims against our gold.

We shall endeavor to administer our operations in such a way that we take dollars away from foreigners whenever and wherever the risk is high of their conversion into gold. Similarly, we shall be willing to put dollars into the hands of foreigners only when the likelihood is small of a conversion into gold.

Dollars held by foreigners become potential claims on our gold reserve only if the foreigners sell them to a foreign central bank.

For this reason, we shall purchase foreign currencies in the open market only if the market situation is favorable, i.e., when dollars are on balance demanded rather than offered. In such a market situation, the other party would probably prefer to hold the dollar proceeds or to use them for its own account, rather than to sell them to a foreign central bank.

If the market situation were unfavorable, the possibility of adding to potential claims on our gold stock would indeed seriously limit our operations in the open market. In such a situation, we shall try to acquire foreign currencies directly for foreign reserve banks by means of a reciprocal transaction. In such direct transactions, we shall be able to minimize the risk that the foreign reserve banks involved would convert their dollar balances into gold.

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Q.3. Would the foreign currencies purchased be redeemable on demand in gold by the countries issuing them?

A.3. The Federal Reserve will deal only in currencies that are fully convertible. Under the Articles of Agreement of the International Monetary Fund (Article VIII, Section 4), these currencies must in general be redeemed upon the request of the Federal Reserve by the central banks of the country of issue either in dollars or in gold.

Redemption in dollars rather than in gold would itself serve to reduce potential claims on our gold stock.

Q.4. It is noted that the primary purpose of this program operating in conjunction with the Stabilization Fund would be to help safeguard the dollar against speculative flows of funds. How will those persons charged with the responsibility of operating this program be able to differentiate between purchases and sales by speculators as against non-speculators and even your own purchases and sales?

A.4. For the purposes of these operations, it would be not necessary for us to attempt to differentiate between purchases and sales of individual speculators and non-speculators. But we shall have the task of differentiating between flows of funds consistent with the underlying economic situation and those representing temporary speculative deviations from that situation.

Admittedly, this task is difficult and subject to errors, but it is not unusual. For example, the manager of the System Open Market Account confronts a similar task from time to time in domestic open market operations.

Experience with foreign exchange operations for account of the Stabilization Fund, which have been conducted by the same officers of the Federal Reserve Bank of New York who will conduct System operations, indicates that it is possible to identify with reasonable accuracy speculative elements influencing the movements of short-term funds and the exchange market.

Moreover, the manager of the System foreign currency account will be helped by the continuous review of the world economic situation conducted by the staffs of the Board of Governors and the Federal Reserve

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Bank of New York, by his close contacts with the New York money and exchange markets, and by continuous consultation with major foreign central banks.

Q.5. What assurances do you have that the net effect of the operation of this program will not in fact be a stabilizing factor for some of the foreign currencies using our dollars instead of trying to stabilize the dollar by using various foreign currencies?

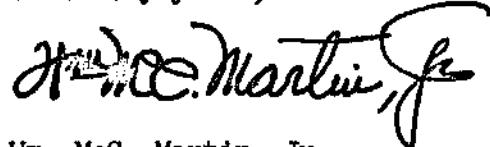
A.5. Any stabilization of the dollar in terms of major foreign currencies will indeed have the incidental effect of stabilizing these currencies in terms of the dollar. This incidental effect, far from being unwelcome, would in itself diminish incentives for speculative activities that might have repercussions adverse to the dollar.

We would not, however, let the operations be used to stabilize a particular foreign currency, the value of which was being undermined by basic financial or economic faults.

Q.6. Please furnish me a chart covering the last ten years showing the relative value of the various foreign currencies purchased or to be purchased in their respective relationship to the value of the dollar.

A.6. I enclose charts showing monthly figures of exchange rates for the six most important European currencies (pound sterling, French franc, Swiss franc, Netherlands guilder, Italian lira and German mark) from 1953 through January 1962. The selections of these charts should not be interpreted, however, as implying that the Federal Reserve intends to operate in all of these currencies or in no others.

Sincerely yours,



Wm. McC. Martin, Jr.

Enclosures



# FEDERAL RESERVE

## press release

For immediate release

March 1, 1962

The Bank of France and the Federal Reserve Bank of New York today agreed on a reciprocal arrangement under which the Federal Reserve Bank of New York will pay to the dollar account of the Bank of France \$50 million against a corresponding payment of approximately 245 million francs to the account of the Federal Reserve Bank of New York with the Bank of France. This arrangement, under which forward cover is provided to both parties, will facilitate official intervention in the foreign exchange market in the event that such intervention may become advisable.

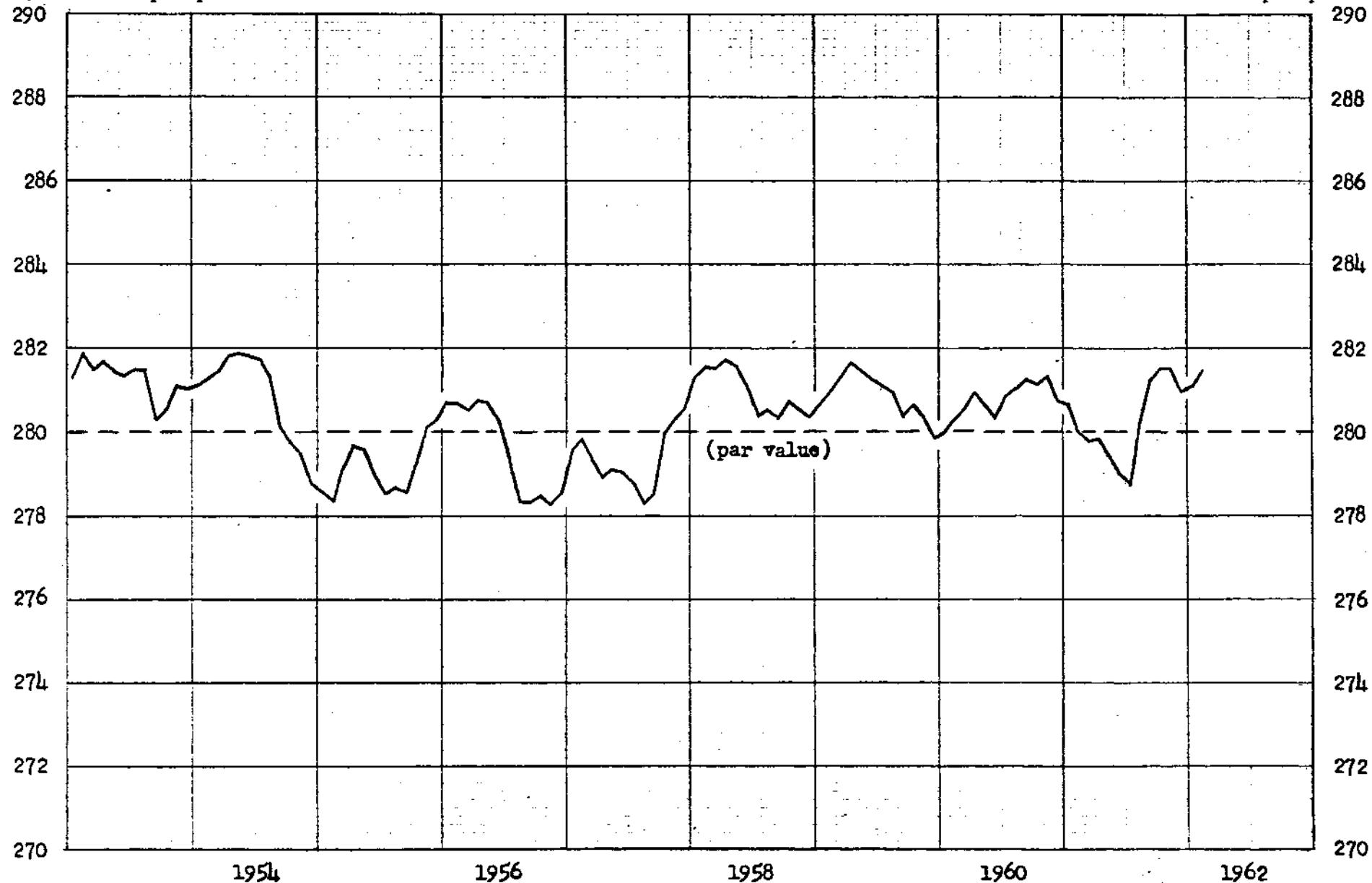
The arrangement, although similar to transactions between the U. S. Treasury and monetary authorities of other European countries, is the first of its kind undertaken since the War by the Federal Reserve System in its own name. The New York Reserve Bank is acting on behalf of the twelve Federal Reserve Banks under the direction of the Federal Open Market Committee.

(Note: The foregoing announcement has also been issued by the Federal Reserve Bank of New York.)

FOREIGN EXCHANGE RATES: UNITED KINGDOM (monthly averages of certified noon buying rates  
in New York for cable transfers)

U. S. cents per pound

U. S. cents per pound



FOREIGN EXCHANGE RATES: SWITZERLAND (monthly averages of certified noon buying rates  
in New York for cable transfers)

U. S. cents per franc

24.2

U. S. cents per franc

24.2

24.0

23.8

23.6

23.4

23.2

23.0

22.8

22.6

22.4

22.2

(gold parity)

1954

1956

1958

1960

1962

FOREIGN EXCHANGE RATES: GERMANY (monthly averages of certified noon buying rates  
in New York for cable transfers)

U.S. cents per deutsche mark

25.6

25.4

25.2

25.0

24.8

24.6

24.4

24.2

24.0

23.8

23.6

U.S. cents per deutsche mark

25.6

25.4

25.2

25.0

24.8

24.6

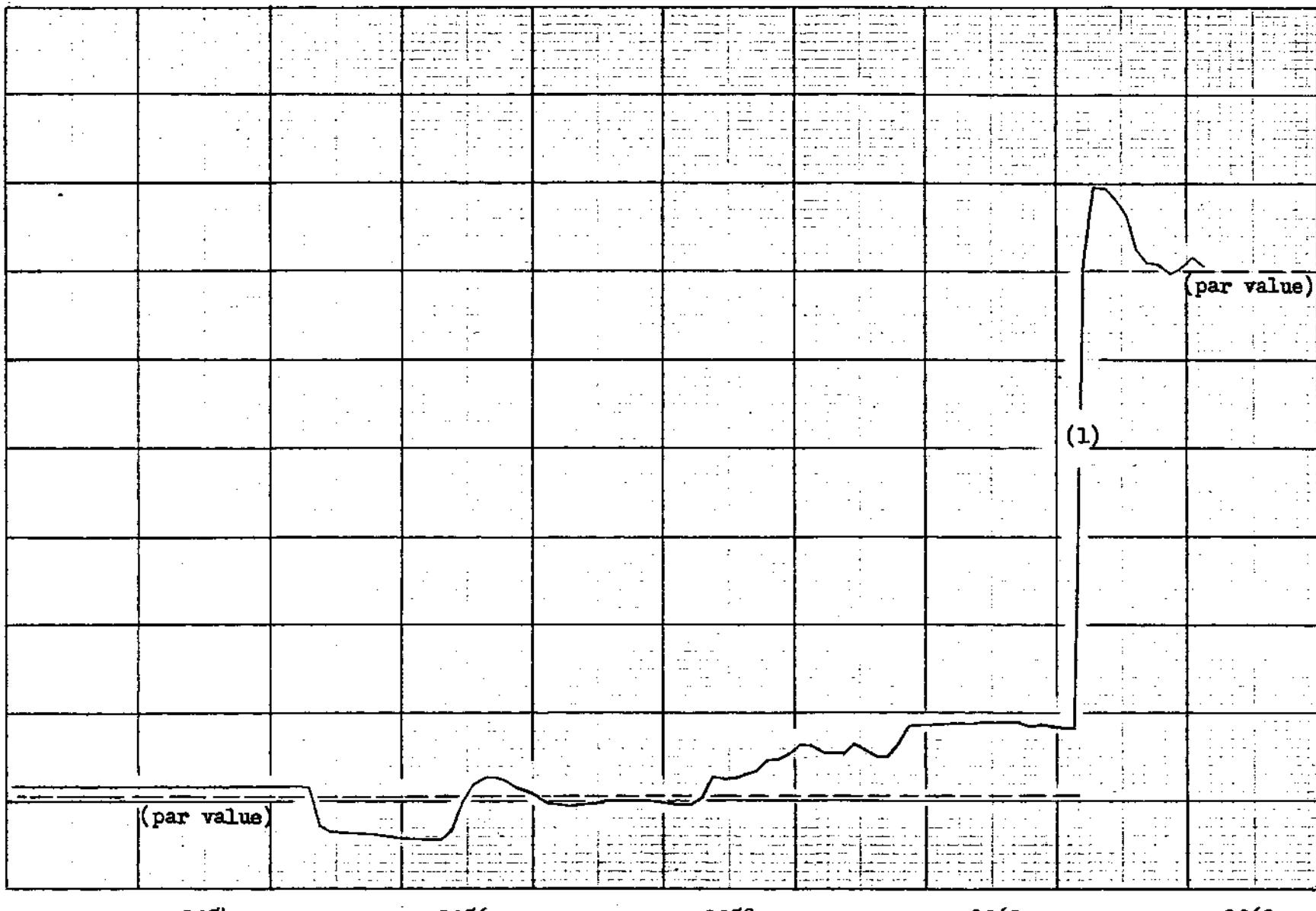
24.4

24.2

24.0

23.8

23.6



1954 1956 1958 1960 1962

(par value)

(1)

(par value)

FOREIGN EXCHANGE RATES: NETHERLANDS (monthly averages of certified noon buying rates in New York for cable transfers)

U. S. cents per guilder

28.0

27.8

27.6

27.4

27.2

27.0

26.8

.6

26.4

26.2

26.0

U. S. cents per guilder

28.0

27.8

27.6

27.4

27.2

27.0

26.8

26.6

26.4

26.2

26.0

(1)

(par value)

(par value)

1954

1956

1958

1960

1962

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(1) Effective March 7, 1961, the par value of the guilder was changed from 26.3158 to 27.6243.

FOREIGN EXCHANGE RATES: FRANCE (monthly averages of certified noon buying rates  
in New York for cable transfers)

U.S. cents per old franc (through December 1959)

U.S. cents per new franc (beginning January 1960)

.288

.286

.284

.238

.236

.234

.206

.204

.202

28.8

28.6

28.4

23.8

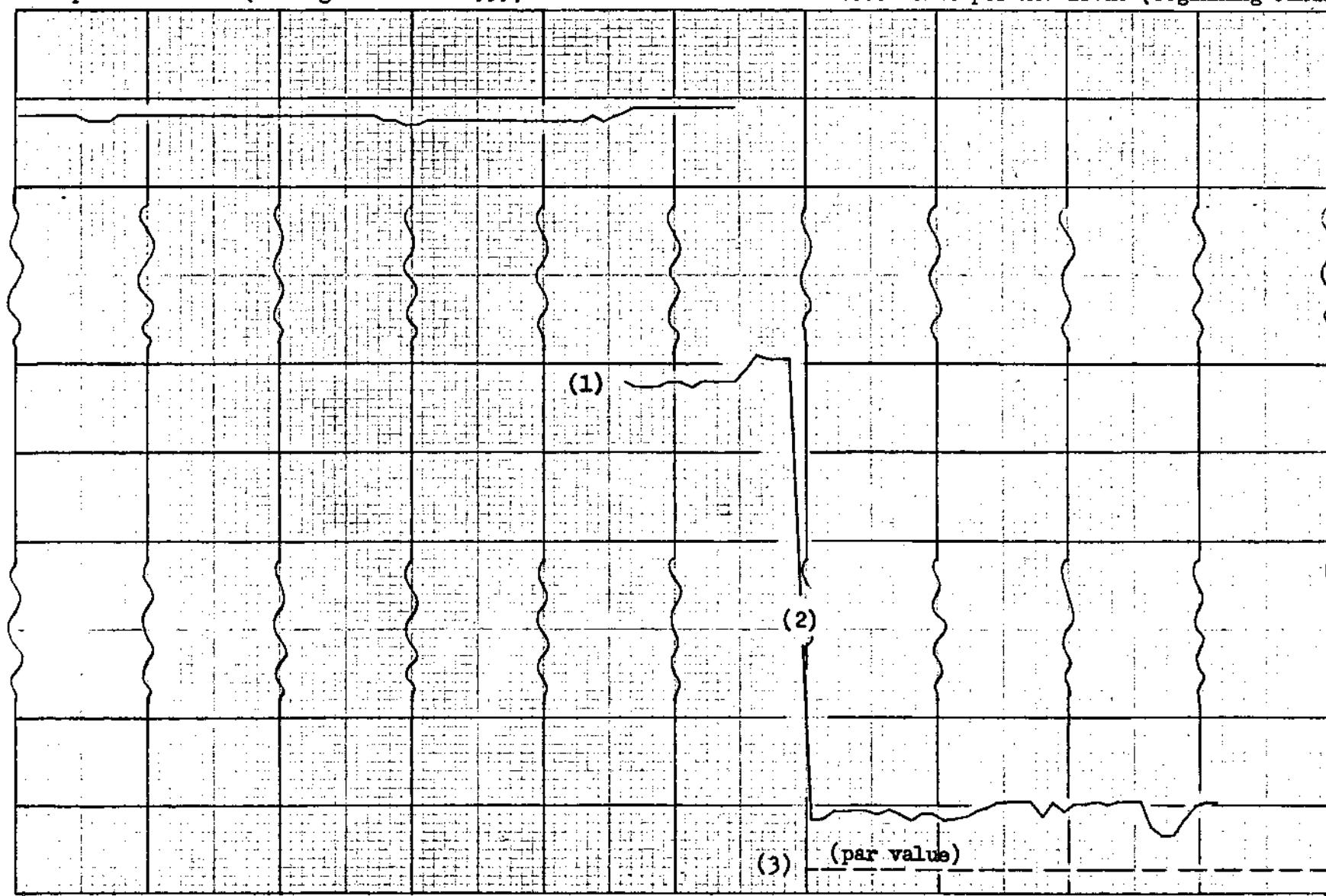
23.6

23.4

20.6

20.4

20.2



1954

1956

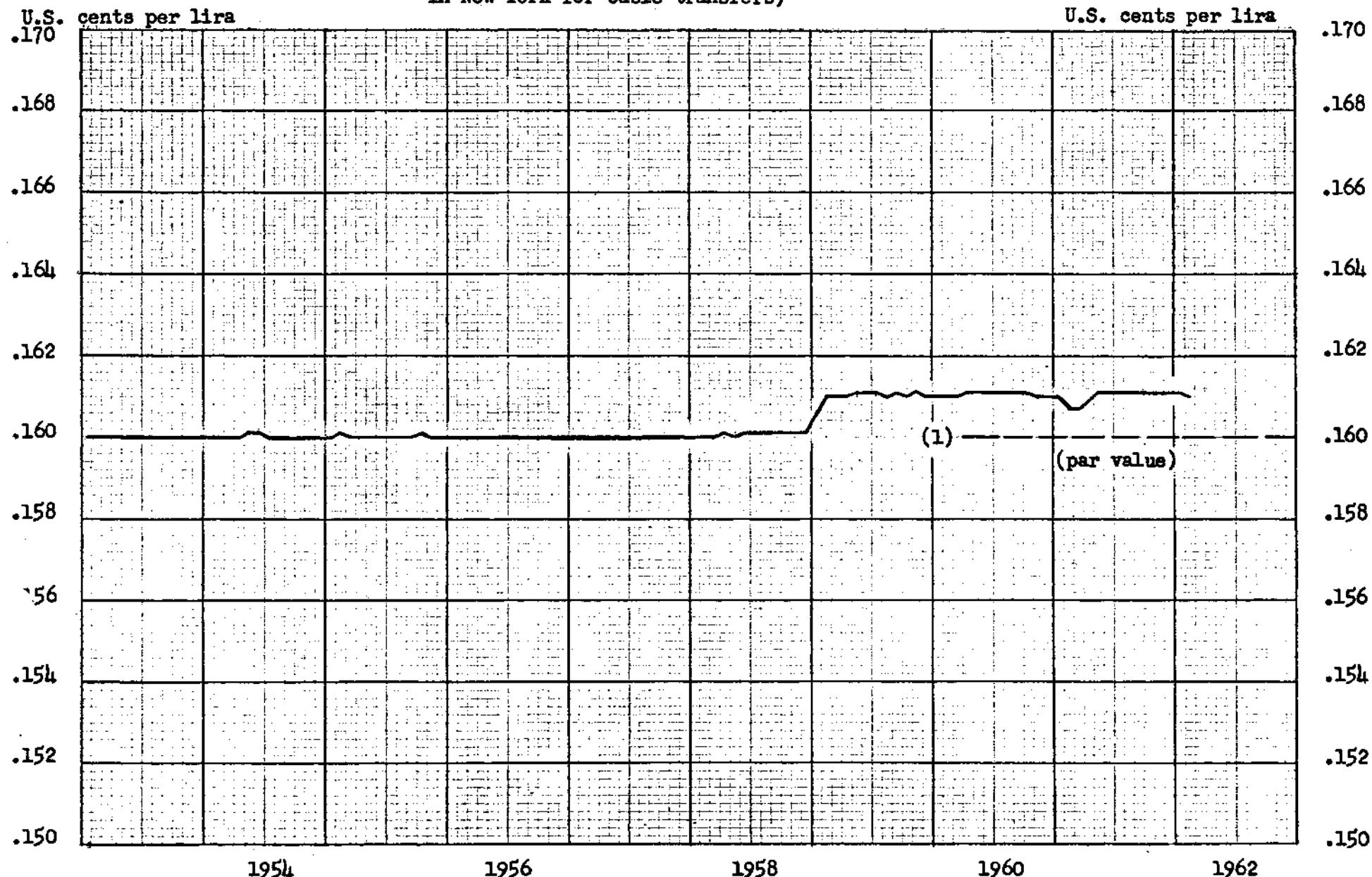
1958

1960

1962

(1) From August 1957 to June 1958, there were two rates. (2) On December 29, 1958, the franc was devalued from .238095 to .202550 U.S. cents. (3) Before December 29, 1958, no par value was agreed with the I.M.F.

FOREIGN EXCHANGE RATES: ITALY (monthly averages of the certified noon buying rates  
in New York for cable transfers)



1954

1956

1958

1960

1962

(1) Before March 30, 1960, no par value was agreed with the I.M.F.

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