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FOR RELEASE TO A.M. PAPERS
FRIDAY, MARCH 12, 1965

PR-24 (3-9-65)

California bankers and businessmen were told tonight that President Johnson is counting on their voluntary cooperation in wiping out the seven year deficit in the nation's international accounts.

The President's message was delivered by Chairman Joseph W. Barr of the Federal Deposit Insurance Corporation in a speech before the Los Angeles Chapter of the American Institute of Banking.

"Probably in no other country in the world today would the head of State, in a matter like this, rest his policy so firmly on voluntary cooperation," Barr said.

"It is no great task," he continued, "to envisage Government directives which would result in a rapid elimination of our payments deficit. But the American way avoids Government directives when possible, and that is just what President Johnson has done.

"The voluntary way, of course, demands that when the Government asks bankers and businessmen to forego certain types of investment opportunities voluntarily in the interests of national policy, all public officials concerned make crystal clear why the request is being made." Outflow of dollars for investment purposes is a major factor, Barr declared, in neutralizing our trade gains.

Substantial improvement in the payments balance this year is imperative, Barr declared. To define the target, he quoted Treasury

Secretary Dillon who said: "We are not thinking of a few hundred million dollars. Even a full billion dollar improvement would not meet our needs. We can and must do considerably more." Barr went on to emphasize that "outside of wartime, the stakes have rarely been higher."

Concluding, Barr declared: "We must not fool ourselves into thinking that because ours is the world's most productive economy, because ours is the world's strongest creditor position, because we have the world's most favorable trade balance, it doesn't matter if we continue to run a deficit in our over-all balance of payments. It matters very much.

"The strength of the dollar rests on the willingness of others to hold and use dollars. For this reason we cannot escape having other governments and other business and financial interests act as constant auditors of our policies and actions. This is simply part of the price of being the Free World's most productive and richest power. It will be true whatever the particular shape of the international payments system."

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RELEASE FRIDAY, MARCH 12, 1965, A. M. PAPERS

BANKING AND THE PAYMENTS DEFICIT

Address of

JOSEPH W. BARR, CHAIRMAN

FEDERAL DEPOSIT INSURANCE CORPORATION

Washington, D. C.

before the

Los Angeles Chapter

AMERICAN INSTITUTE OF BANKING

Los Angeles Club

Los Angeles, California

Thursday, March 11, 1965

Dinner Meeting

Address of
Joseph W. Barr, Chairman, Federal Deposit Insurance Corporation
Before the Los Angeles Chapter of American Institute of Banking
Los Angeles Club, Los Angeles, California
Thursday P. M., March 11, 1965

BANKING AND THE PAYMENTS DEFICIT

I am going to use your kind invitation for me to come here to perform an urgent errand of public business. President Johnson has asked all of us who are concerned with the financial health of this country to carry across the land the message of his determination to wipe out the deficit which for the past seven years has appeared in our international accounts. And he is counting on your cooperation to get this job done quickly and with a minimum of dislocation in the normal affairs of business, banking, and Government.

Perhaps some of you were at the White House last month and heard the President say to a group of business and banking leaders: "I hope that you will feel that you can join your government in a new and I believe a bold attack on this problem." Probably in no other country in the world today would the head of State, in a matter like this, rest his policy so firmly on voluntary cooperation. It is no great task to envisage Government directives which would result in a rapid elimination of our payments deficit. But the American way avoids Government directives when possible, and that is just what President Johnson has done.

The voluntary way, of course, demands that when the Government asks bankers and businessmen to forego certain types of investment opportunities voluntarily in the interests of national policy, it behooves all public officials concerned to make crystal clear why the request is being made. This, the President and Secretary Dillon have done. I want tonight to bring their explanation directly to you.

If you study the international accounts of the United States as you study the accounts of your business clients, you would have every right to scoff at the idea that there was a pressing problem before us. You would look at the growth of U. S. assets abroad over the past several years, and you would find that between 1950 and 1963 they increased from $31 billion to no less than $88 billion. In the same period, our liabilities to foreigners increased from $17 billion to $51 billion. So our net assets increased by $23 billion over that thirteen-year period. Over the same period you would note that our gold reserves had declined by about $7 billion. This ratio of gold use -- or the use of liquidity or current assets, if you will -- to capital acquisition is certainly a healthy one. This is why the President said in his message to Congress: "the strength of the dollar is backed by the world's strongest creditor position."

Now if we were talking about a private business and not a government, there would be no problem. After all, when a business is as solid as is suggested by those figures I just cited, no bank is going to fail to lend money to cover a deficit on current operations. But when the United States runs a large over-all payments deficit for seven successive years, you have to expect that, for good reasons or bad, some other governments may reach the point where they decide that they are holding enough dollars and prefer to cash in additional dollar acquisitions for gold.

Now why do we have a deficit? Let's look at the current account. First, take the trade account. In the past four years our commercial exports have risen by $4.9 billion, or about 28 percent. Our imports have gone up, too, as was to be expected in our growing economy. But in 1964 we sold abroad $3.8 billion more than we bought. Our commercial trade surplus was $1.5 billion greater in 1964 than in 1963. No wonder President Johnson told the Congress that the United States has "the world's strongest trade position."

Here let me digress a bit to pay tribute to the State of California -- the nation's number one exporter. In 1963 -- the latest year for which figures by State are presently available -- your factories, farms, and mines exported significantly more than $2 billion worth of goods. Your manufacturers, who accounted for slightly less than three quarters of the total, ranked third in the nation and increased their export sales by 11 percent between 1960 and 1963. Your electrical machinery manufacturers nearly doubled their exports in those three years. Your exporters of processed foods showed a 25 percent increase. And your aircraft factories, of course the biggest exporters in California, continued to earn better than half a billion dollars abroad each year.

If the balance of payments problem is just an export problem, don't tell it to the Californians! You have every right to be proud of your contribution to the strength of the dollar.

Need I add that exporting has been good for California, too? Projecting from 1960 figures, conservatively half a million factory workers in California today owe 10 percent or more of their pay checks to exports. At least the equivalent of 50,000 California farmers owe their livelihood to exports. But you know all this. The more than $100 million you have invested in expanding the ports of Los Angeles and San Francisco in recent years is testimony enough.

But back to our current international account. While our favorable trade balance has been growing, current earnings on our overseas investments have also been rising rapidly, amounting to $4.8 billion in 1964. On Government account, last year our military and other security interests abroad resulted in a deficit of about $2.7 billion. These are dollars we spend to maintain military forces abroad and for that portion of foreign aid (about 15 percent) which is not tied directly to purchases of U. S. goods and services. As Secretary Dillon detailed before the National Industrial Conference Board meeting in Washington last month, these items in the balance of payments have been subjected to unremitting scrutiny from various Government departments over the past four years and consequently have been steadily shrinking. "By a drastic policy of tying foreign aid expenditures to U. S. goods and services," Secretary Dillon said, "we have saved almost $500 million. We have cut military outlays abroad by more than $200 million -- despite sharply rising prices in the countries where our forces are stationed -- and we have increased sales abroad through the Defense Department by another $450 million."

If any of you were in Washington to hear the President last month, you know he has given the strictest kind of orders to his cabinet officers to find further ways, consistent with national security, to shrink that portion of the deficit which is attributable to Government programs. But I don't have to tell you that it would be short-sighted in the extreme to sacrifice vital American military and political interests in this cause. Protection of the dollar cannot be safely bought at the sacrifice of vital security positions.

If you add up the increase in our trade surplus since 1960, the increase in investment income, and the savings made on Government account, you have enough, all else aside, to wipe out the deficit which existed in our balance of payments in 1960. "Our problems today," as Secretary Dillon put it, "arise from the fact that the full force of these gains has, thus far, been largely neutralized by a $2.5 billion boost in private capital outflows since 1960 -- $2 billion of which happened last year."

On top of this, the expenditures of American travelers and tourists abroad last year were $600 million higher than in 1960, over twice the increase in the expenditures of foreign travelers and tourists here. The American wanderlust contributes no less than $1.6 billion to our payments deficit. No wonder the President urged Americans to go West for vacation this year -- or, excuse me, in California I should say: "Go East!"

Now, as I said a moment ago, it wouldn't be difficult to devise Government directives which would very quickly staunch these outflows. The Government could tax tourists going abroad in one way or another. It could give a hard twist to the screws of monetary policy. It could put rigid controls on capital going abroad in search of a profit. Most of you no doubt have read suggestions like these in the press in recent weeks. But the President has courageously and confidently chosen a different course.

Taxes on tourists and travel are inevitably discriminatory. This course was rejected.

Similarly, official restrictions and complex bureaucratic controls on the movement of private capital are anomalies to be avoided whenever possible under our free enterprise system.

To be sure, the President has ordered some direct Government action. Congress has been asked to limit to $50 the amount of duty-free goods tourists can bring back with them from their travels. The Interest Equalization Tax is to be renewed and has been extended to cover bank loans to foreigners with maturities of one year or more. (As you are aware I am sure, this tax does not apply to export-connected loans or to loans to borrowers in the so-called underdeveloped countries.) But the President and Secretary Dillon have left no doubt that it is not these limited Government directives, but rather the voluntary cooperation of American business and finance which will determine the success or failure of the campaign to wipe out the current payments deficit.

The President also rejected the so-called classical cure for a payments deficit -- that is, a sharp hike across the board in interest rates. As you are well aware, short-term rates have risen nearly 1-3/4 percent over the past three years and Federal Reserve discount rates have been raised by 1 percent -- as part of the balance of payments strategy. But the President is determined to maintain ample amounts of long-term credit available for domestic expansion; he was not willing to prescribe the conventional, outmoded, deflationary cure. The President's Great Society policy rests on ample credit, and a budget balanced at a high level of economic activity.

By this process of elimination, the President arrived at his bold and confident appeal to the business and banking community to work with him voluntarily to wipe out the deficit in our current payments. He said to the assembled bankers and businessmen in Washington, "I want you to go back to your offices and call to your desk your financial men and your economists and your comptrollers and your vice presidents and I would hope that you will ask them in a reasonable way to consult with you every time they face a decision that involves sending money abroad." The President added, "I know this will involve some pain. I know it will involve some sacrifice and it will mean passing up some opportunity for additional profits. But in the end I earnestly believe that your country and your industry and your stockholders will be the better for it."

Surely there is no question but that the United States must show a substantial improvement this year in its payments balance. Secretary Dillon defined the target this way: "We are not thinking of a few hundred million dollars. Even a full billion dollar improvement would not meet our needs. We can and must do considerably more." Outside of wartime, there have been few more exacting tests than this of what the President calls "our Government-business partnership in America." But outside of wartime, the stakes have rarely been higher. The strength of the international payments system depends not just on the long-term prospects of the dollar, but on the short-term prospects as well. After seven years of deficits, we must move more rapidly toward equilibrium in our international accounts.

This international payments system we have is, perhaps, not a thing of artistic beauty, and it inevitably attracts the barbs of several kinds of critics. Recently one would think that an open season for critics has been declared. One school would restore to gold its former function as the automatic arbiter of economic policies; "return to the gold standard!," they say, "when settling debts among nations was so much simpler" -- and so depressing. At the same time, another school urges us to do away with gold altogether; in the opinion of these critics, the idea of gold as a socially useful device belongs somewhere back in the Old Testament.

We will probably all live to see changes in the present payments system. In his message to the Congress President Johnson said: "For some time we have been exploring with our major trading partners how best to create new reserve assets that will be available to supplement gold and dollars. We must press forward with our studies and beyond to action .... evolving arrangements which will continue to meet the needs of a fast growing world economy." These words of the President's are a guarantee that this Administration will be prepared for whatever creative changes careful study may show to be necessary.

A step in this direction was taken on Friday, February 26, when the Executive Directors of the International Monetary Fund agreed to propose an increase of 25 percent in the quotas of member countries. If all countries avail themselves of this increase, the total quotas in the Fund would rise from $16 to $21 billion. This action was taken because the Executive Directors concluded that in a world in which income and trade have expanded rapidly and are expected to continue to do so, the need for the type of liquidity supplied by the Fund may be expected to grow.

The special policies and procedures worked out to mitigate the effects of the 25 percent gold payment on the reserve countries, the United States and the United Kingdom, constitute solid evidence of a continuing spirit of cooperation among the financial leaders of the Free World.

However, we should be under no illusion that cooperation or reform can substitute for the discipline we must establish at home.

We must not fool ourselves into thinking that because ours is the world's most productive economy, because ours is the world's strongest creditor position, because we have the world's most favorable trade balance, it doesn't matter if we continue to run a deficit in our over-all balance of payments. It does matter. It matters very much. As bankers you all know that, in the last analysis, the dollar is strong because people have confidence in it. Continued large deficits in our balance of payments -- after seven years of such deficits -- can erode that confidence. We cannot let that happen, because we -- and the international economy -- are dependent on a strong and unquestioned dollar.

The strength of the dollar rests on the willingness of others to hold and use dollars. For this reason, we cannot escape having other governments and other business and financial interests act as constant auditors of our policies and actions. This is simply part of the price of being the Free World's most productive and richest power. It will be true whatever the particular shape of the international payments system.

Just as American power abroad is the major element in keeping the peace of the world today, so the dollar is the key currency in world trade and investment. We derive both wealth and prestige from this fact; it is an inevitable concomitant of world leadership. With this comes the responsibility to live according to the rules. To do so through a voluntary partnership of Government and business and finance is the American way. I am confident that in the months ahead this partnership will function in such a way as to command renewed respect from the world around us.

The President has assigned the primary operating responsibility for implementing hisprogram to the Secretaries of Treasury and Commerce and to the Federal Reserve Board. The President has directed me to cooperate completely with these agencies, and I intend to do so. Let me assure all of you in the banking community of this State that my help and the help of the Corporation is always available to you as we move forward in this crucially important program.

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