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Statement by

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before the

Commerce, Consumer, and Monetary Affairs Subcommittee

Committee on Government Operations

House of Representatives

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I am pleased to appear today to testify in connection with your examination of the investments in the United States of the countries that are members of the Organization of Petroleum Exporting Countries (OPEC), especially the Middle Eastern OPEC countries. I should like to begin with a brief review of the changes in foreign official holdings of foreign exchange reserves in recent years, and especially since the major rise in oil prices in 1973-74, to provide a framework for an evaluation of the scope of the increase in OPEC reserves over that period. Then I will take up the particular issues that you have identified.

One of the striking phenomena of the international economic scene over the past decade has been the quantum jump in the amount of foreign exchange reserves of foreign countries. As shown in the first table, such assets rose from $45 billion at the end of 1970 to nearly $300 billion by the end of March this year, an increase of over $250 billion. The share of OPEC countries in this growth has been substantial; their reserves as recorded by the International Monetary Fund have risen from less than $5 billion in 1970 to $53 billion at the end of March 1979, with by far the greatest amount accruing to OPEC countries located in the Middle East. Even though they have enjoyed large increases, however, it is evident that the increase in the foreign exchange holdings of the OPEC countries accounted for only about one fifth of the total increase for the period recorded by the IMF. Moreover, the reserves of the OPEC countries reached a peak in 1977 and declined during 1978 as their surplus diminished. Of course, that declining trend is now being reversed.

Over the years since 1970 about half of the reported official foreign exchange reserves of other countries has been held directly in the United

States -- about $24 billion in 1970 and $153 billion at the end of March 1979. Of the latter figure, about $21 billion is held by OPEC countries. I should note that these figures cover primarily money market assets and U.S. Government debt - those kinds of assets that are most readily susceptible to liquidation. An additional amount of $34 billion of foreign official reserves is held at the foreign branches of U.S. banks, and OPEC countries account for about two thirds of those holdings.

The rise in foreign official holdings of foreign exchange over the years has reflected a combination of factors. One element has been the wish of foreign authorities to strengthen their reserve positions as the nominal value of international trade and other transactions rises, so as to have a cushion against adverse developments. A large part of the increase is the result of efforts on the part of some countries to avoid appreciations of their currencies, that is, to support the value of the dollar, at times when the U.S. dollar has been under downward pressure in the markets. For many OPEC countries, there is the additional factor that for various reasons they are unable to spend all of the proceeds of their accelerating oil export revenues, and must find an outlet for their savings in relatively safe and liquid assets that provide a current and future stream of income.

The flow of OPEC funds into reserve assets has varied with the changes in their investible surplus. We have seen no indication that the timing or choice of investments has reflected any factors other than those that prudent investors normally take into account. Last year, when the overall OPEC surplus dropped below $5 billion, and there was a corresponding drop in the rate of acquisition of foreign exchange, there may have been some diversification into non-dollar denominated assets. However, we have no evidence indicating that these countries' actions were a major factor in foreign exchange markets.

The substantial increase in the amount and share of U.S. Government securities held by foreign monetary authorities has increased the degree to which Federal Reserve and Treasury market operations may at times have to take account of foreign developments. For example, the Treasury at times in the early 1970s and again in 1977-78, after consultation with Federal Reserve officials, issued special securities to foreign governments and placed the proceeds temporarily in deposits with commercial banks to avoid draining reserves from the banking system.

From January to April of this year, foreign official holdings of Treasury securities declined by $17 billion (table 2), reflecting heavy sales of dollars in foreign exchange markets by a number of foreign countries, notably Germany and Japan. In this four-month period foreign official holdings of Treasury bills declined from 42 percent of the total outstanding bill supply to 31 percent, and Treasury bill rates rose relative to other U.S. short-term rates. This shift in bill holdings and rise in bill rates tended to restore interest-rate relationships of earlier years, and no special action by the Federal Reserve or Treasury was deemed necessary. If foreign sales of bills or other securities had threatened to disrupt the markets for these instruments, the Federal Reserve could have undertaken market actions to moderate the impact.

We are accustomed to facing a situation in which a number of countries, whether OPEC or other countries, might wish to dispose of large amounts of Government securities. Based on our experience, we are confident that the regular procedures that are available to us, and that have been tested on a number of occasions, are adequate to deal with any such contingencies, so that we do not believe that a formal contingency plan is necessary. However, we maintain close vigilance over actual and potential dealings of foreign official accounts in this market so that our procedures for accommodating them can be implemented at the right time.

With respect to foreign accounts in U.S. banks, withdrawals of foreign official funds from one or a group of U.S. banks would in all likelihood be met by adaptations within the commercial banking system itself. The most likely and direct consequence of such a withdrawal would be that U.S. banks losing deposits would borrow them back from the foreign banks that had received them. There simply would be no other important outlet for such a supply of liquid dollar funds by foreign banks in a short period. It is important to note, however, that American banks would sustain a financial loss in the process, since they would have to pay the foreign banks for the service they would be performing as intermediaries. Another adjustment available to banks that lost deposits would be to sell some of their assets to the banks receiving the deposit inflow.

While we would expect that the banking system could adjust to large withdrawals of funds through market transactions without major disruptions, in the event any particular member bank were to be hit by liquidity difficulties because of any abrupt withdrawal of funds it could obtain short-term credit through the Federal Reserve's discount window.

Because these mechanisms are available to deal effectively with massive shifts of funds from U.S. banks we have not undertaken any special studies or analyses dealing with this aspect of OPEC investments in the United States. However, we have a close and continuing interest, through our regulatory and supervisory responsibilities, in the vulnerability of U.S. banks with respect to their relationships with individual customers. We have not singled out any particular class of borrower in this process, but we have established certain guidelines for the examination process that would apply to OPEC countries as well as others.

Your request for information on the amount of OPEC deposits in and loans from domestic and foreign branches of American banks for each individual OPEC country raises important policy questions, as you are aware. Let me begin by noting the two main sources of data on this subject. First there are the data collected by the Treasury (with the Federal Reserve acting as collecting agent) covering the foreign assets and liabilities of banking offices in the United States. The Treasury establishes the procedures to be followed in collecting and disseminating such data. The second system covers the assets and liabilities of the foreign branches of U.S.-chartered banks, and has been established by the Federal Reserve in connection with its supervisory and regulatory responsibilities. Data from the two systems are designed to supplement each other.

With respect to banks' liabilities to foreigners, it is long-standing U.S. policy to release details of the statistics only to the extent that doing so does not reveal activities of individual banks or their customers. In connection with the data for which they are responsible, the Treasury has indicated that pursuant to that limitation the holdings of individual OPEC countries in U.S. offices of banks may not be released, since for these countries all but a small part of the total is held by official agencies of those countries. In collecting and publishing the data on foreign liabilities in the foreign branches of U.S. banks the Federal Reserve has applied the same policy concerning the publication of data for individual countries. The proportion of OPEC deposits in these branches that is held by official agencies of those countries is comparable to the proportion in their accounts in U.S. head offices. We believe that it is proper to preserve the confidentiality of individual depositors, and we apply this policy uniformly, with no special consideration for OPEC countries. Furthermore, although our data collection system for branch data does not operate under the direct authority of the International Investment Survey Act of 1976, 22 U.S. C. 3101 et seq., we believe it is appropriate to follow the procedures for disclosure established in that Act. We have a number of other reasons for taking this position:

First, the reputation and effectiveness of the U.S. dollar as a world reserve and transactions currency rests to some extent upon the free convertibility, exchangeability, and use of the dollar abroad unfettered by exchange controls or personalized reporting. The publication of data violating this trust would reflect upon the use of the dollar in the future and perhaps compromise its international role.

Second, we should recognize that the Federal Reserve System publishes far more information in this area than any other major central bank, both in depth of data and timeliness of release. Since we have assured you that the OPEC deposits do not constitute a present threat to our financial system, and the GAO confirms this position, we fail to see why publication of individual country data for OPEC satisfies an essential interest, while it opens up the substantial risks of breaching our statistical rules on privacy, potential withdrawal of accounts, and establishing another competitive disadvantage for U.S. banks.

Finally, I believe that such individualized reporting could hamper the Federal Reserve System's relations with other central banks at a time when we have been one of the leaders in developing new cooperative statistical releases among the major central banks. If we were forced to release data on foreign transactions or deposits against the wishes of the host country, the central bank of that country would likely be much less willing to provide detailed reports to us or to cooperate in new informational data releases. We view such a potential development as a serious setback to the much broader aim of providing steadily more information to all participants. Indeed our current efforts to find ways to share information on troubled banks between countries which have units of the same bank could be blocked by a loss of trust in our ability to hold data on a confidential basis.

While we cannot supply data in the detail you request, we have compiled data (table 3) showing the deposits of Middle East oil-producing Countries in the foreign branches of major U.S. banks. In this compilation we have followed the format that was developed in December 1975 in order to provide data requested by the Subcommittee on Multinational Corporations of the Senate Foreign Relations Committee. For that purpose we grouped U.S. banks into three sets of banks constructed so as to avoid disclosure of the positions of individual banks or of individual OPEC countries. In the updated compilation we are able to show both the absolute growth in OPEC deposits at the foreign branches of these groups of major U.S. banks between 1975 and March 1979, and also the share of these deposits in the total deposit liabilities of these banks. Deposits of OPEC countries with the branches account for over 70 percent of their total deposits in U.S. banks. These tabulations show that at the end of March this year deposits of the Middle East oil-producing countries with the six largest banks as a group amounted to 6 percent of their consolidated deposit liabilities, compared to 5 percent at the end of 1975. These banks have the great bulk of OPEC deposits; both total OPEC deposits and the ratio of OPEC to total deposits are much lower in the two groups of smaller banks. In all, nine banks had liabilities to this group of OPEC countries amounting to one percent or more of their consolidated total deposits.

We have also compiled data (table 4) on the number of U.S. banks in which each of the OPEC countries maintains deposits. (Our data are based on the reports we have for deposits in foreign branches, where the bulk of OPEC deposits are held.) That tabulation shows that most of the OPEC countries maintain deposits at the foreign branches of thirty or more U.S. banks, and none uses fewer than ten U.S. banks. As I have noted above, however, the amount deposited tends to be concentrated in the six largest banks.

We have no record of any discussions with representatives of OPEC countries bearing on the question of whether they might be influenced to remove their assets from U.S. banks if data for accounts of their countries in the United States were published separately. However, although we cannot cite specific documents, we understand that many of the OPEC countries have expressed their sensitivity to disclosure of their accounts to the banks with whom they do business. This issue was thoroughly explored in 1975 in connection with the Senate inquiry to which I have already referred. We have no record of any representation by the Treasury or other Agencies to the effect that data for these countries should be given special treatment because of such sensitivity. Nevertheless, knowing that such sensitivity exists for all countries, and probably in great degree for the OPEC countries, we believe that revelation of data for individual countries, involving as it would an unwarranted disclosure of confidential information about holdings of their official agencies, could cause those countries to divert their assets to deposits or other assets in other countries and other currencies.

As I have said, we believe the mechanisms are in place to deal with possible diversions of funds, so that we would not be confronted with a crisis for our financial institutions or our credit markets. I must emphasize, however,that if the confidentiality of these asset holdings is not preserved there could well be lasting and significant damage to the ability of U.S. banks to compete internationally, and to the status of the dollar as a vehicle in which foreigners, both official and private, could hold their reserves and transactions balances.

A different situation prevails with respect to the compilation and release of data on loans to foreign borrowers by U.S. banks, and by commercial banks in general. We believe that the overriding concern here is to ensure that the public, and banks in particular, are as fully informed as possible about the financial condition of potential borrowers. To meet that responsibility the Federal Reserve and other regulatory agencies have been developing detailed statistics on foreign lending by U.S. banks, consolidating the claims of the head offices and foreign officies of the banks. I have attached to my statement a table (table 5) giving the data for individual OPEC countries. Some additional details are given in the press release containing the complete tables. Our table shows that U.S. banks' claims on OPEC countries reached $20 billion, in total, at the end of 1978, of which $8.2 billion was claims on public bodies.

The largest OPEC borrowers were Venezuela, Iran, Indonesia and Algeria. For comparison, similar claims on non-OPEC developing countries amounted to $52 billion at that date.

You ask whether the Federal Reserve has any reason to believe that any OPEC money has been deposited in banks, invested in bank equity, or been used to purchase U.S. Government securities, through third party nominee/custody accounts. We have no specific evidence of such indirect placements or their extent, but the use of financial intermediaries by all classes of foreign investors is so common that we would also expect to find that OPEC countries use such channels from time to time. For example, the Treasury study "Foreign Portfolio Investment in the United States" shows that in 1974 out of a total foreign investment in U.S. corporate stocks valued at about $24 billion, over half ($13 billion) was reported as being held for the account of foreign bankers, brokers and nominees.

The fact that the use of such intermediaries makes it difficult to have precise information on the country distribution of beneficial ownership of foreign-owned assets in the United States has been well known for many years. Consideration has been given to the possibility of going beyond the present reporting requirements for financial institutions to try to identify the persons for whom transactions data are reported, but no practical way of achieving such an identification has been developed. The situation has been made even more difficult by the growth of the facilities of offshore markets in Europe and elsewhere for dollar-denominated deposits and securities. Apart from the difficulty of tracing the chain of transactions and ownership through which such activities are often conducted, the initiation of such an effort, which would require the cooperation of foreign financial institutions, would probably in itself cause foreign investors who wish to protect the confidentiality of their investments to shift away from institutions that come under the jurisdiction of the United States. We would probably reduce the amount of information available to us if we took measures that induced investors to use offshore financial markets to a greater extent than at present.

I believe my comments have covered all the questions you have raised. We have developed data that we hope will be of assistance to your Committee in its study of these issues. I regret that we could not provide some of the detailed data you specifically requested, but I trust you will understand the circumstances that limit our ability to do so.

TABLE 1

FOREIGN OFFICIAL RESERVES OF FOREIGN EXCHANGE
(billions of dollars)

	December 1970	December 1973	December 1977	December 1978	March 1979
I. Total Holdings	45.4	122.4	243.0	283.3	298.0
A. OPEC countries	3.6	12.6	67.9	53.0 1/	53.2 1/
1. Middle Eastern 2/	2.5	8.5	52.4	41.7 1/	42.2 1/
2. African 3/	0.3	1.3	5.3	3.2	3.4
3. Other 4/	0.7	2.6	9.6	8.1	7.6
B. All other countries	41.8	109.8	175.1	230.3	244.8
II. Holdings in the United States	23.8	66.9	131.1	162.4	153.3
A. Treasury bills and certificates	13.4	31.5	47.8	67.7	59.7
1. OPEC countries 5/	n.a.	n.a.	4.2	3.3	3.2
2. Other countries	n.a.	n.a.	43.6	64.4	56.5
B. Marketable Treasury bonds and notes	0.3	5.7	32.2	35.9	36.0
1. OPEC countries 5/ (approximate)	n.a.	n.a.	11.0	9.0	8.0
2. Other countries	n.a.	n.a.	21.2	26.9	28.0
C. Nonmarketable Treasury bonds and notes 6/	3.4	15.5	20.4	21.0	20.5
D. Other U.S. securities	0.7	1.7	12.7	14.7	14.9
E. Banking and money market assets 7/	5.9	12.4	18.0	23.1	23.2
1. OPEC countries	n.a.	n.a.	9.6	10.2	9.8
2. Other countries	n.a.	n.a.	8.4	12.8	13.4
III. Holdings at Foreign Branches of U.S. Banks	4.2	10.3	28.1	31.9	34.1
A. OPEC countries 5/ 8/	n.a.	n.a.	19.1	20.1	23.1
B. Other countries	n.a.	n.a.	9.0	11.8	11.0

1/ Beginning April 1978 data exclude Saudi Arabian foreign exchange cover against the note issue (amounting to about $5.3 billion in March 1978).
2/ Iran, Iraq, Kuwait, Libya, Qatar, Saudi Arabia, United Arab Emirates.
3/ Algeria, Gabon, Nigeria.
4/ Ecuador, Venezuela, Indonesia.
5/ Also includes Bahrain and Oman.
6/ None held by OPEC.
7/ Principally bank deposits, CDs, repurchase agreements, bankers acceptances, and commercial paper.
8/ Including some private holdings.

Sources: I.: International Monetary Fund, *International Financial Statistics.*
II.: U.S. Treasury.
III.: Federal Reserve System.

TABLE 2

FOREIGN OFFICIAL HOLDINGS OF MARKETABLE U.S. TREASURY SECURITIES, SELECTED DATES

	Amount ($ billions)			Percentage of total outstanding		
	Bills	Bonds & Notes	Total	Bills	Bonds & Notes	Total
1968 - November	6.5	.5	7.0	8.9	0.3	3.0
1969 - June	3.8	.5	4.3	5.6	0.3	1.9
1973 - March	37.6	6.9	44.5	35.8	4.2	16.5
1974 - January	29.2	5.2	34.4	27.1	3.2	12.7
1979 - January	68.4	36.0	104.4	42.1	10.8	21.0
- April	51.3	36.3	87.6	31.3	10.7	17.4

TABLE 3

DEPOSITS OF MIDDLE EAST OIL PRODUCING COUNTRIES
IN FOREIGN BRANCHES OF LARGE U.S. BANKS
(billions of dollars)

	December 1975			March 1979		
	Six Largest Banks	Second Largest Six Banks	Next Nine Banks	Six Largest Banks	Second Largest Six Banks	Next Nine Banks
(1) Total deposits (consolidated)	197.5	76.3	49.9	273.8 1/	99.9 1/	68.4 1/
(2) Deposits of Middle East Oil Producing Countries 2/	9.8	1.2	0.7	16.3	1.7	0.5
(3) Line (2) as percent of Line (1)	5.0	1.6	1.4	6.0	1.7	0.7

Note: Deposits in foreign branches represent more than 70 percent of total deposits of Middle East oil producers in all U.S. banks.

1/ Deposits as of Dec. 1978.
2/ Includes Iran, Iraq, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates.

Six largest banks	Second largest	Next nine
Bank of America	Bankers Trust	European American Bank & Trust
Chase Manhattan	Continental Illinois	First National Bank of Boston
Chemical Bank	Crocker National Bank	First National Bank of Dallas
Citibank	First National Bank of Chicago	First National Bank of Detroit
Manufacturers Hanover	Security Pacific	Irving Trust
Morgan Guaranty	Wells Fargo	Marine Midland
		Mellon
		Republic National Bank, Dallas
		United California Bank

TABLE 4

NUMBER OF U.S.-CHARTERED BANKS REPORTING LIABILITIES TO OPEC COUNTRIES AT FOREIGN BRANCHES

	Dec. 1975	Dec. 1976	Dec. 1977	Dec. 1978	Mar. 1979
Ecuador	31	36	46	45	39
Venezuela	80	82	89	81	88
Indonesia	48	52	50	43	45
Iran	40	50	53	50	49
Iraq	11	23	24	13	13
Kuwait	28	30	33	29	32
Qatar	17	8	15	17	16
Saudi Arabia	18	30	31	33	34
United Arab Emirates	19	24	34	38	37
Algeria	36	44	45	51	51
Gabon	16	19	26	19	19
Libya	9	15	14	12	11
Nigeria	11	14	13	19	19

TABLE 5

U.S. BANKS' CLAIMS ON OIL-EXPORTING COUNTRIES
(millions of dollars)

	Dec. 1976	June 1977	Dec. 1977	June 1978	Dec. 1978	
					Total	Public borrowers
Total	12,394	12,163	14,686	16,542	20,047	8,197
Algeria	1,234	1,470	1,541	1,540	1,830	1,111
Ecuador	660	831	1,040	1,360	1,561	697
Gabon	126	n.a.	185	208	225	207
Indonesia	2,067	1,980	2,199	2,238	2,215	922
Iran	1,390	1,831	2,202	2,266	2,626	945
Iraq	73	88	93	86	155	38
Kuwait	371	399	536	504	779	2
Libya	110	128	58	81	139	5
Nigeria	70	70	129	409	619	358
Qatar	32	81	73	126	176	112
Saudi Arabia	600	336	592	735	918	48
United Arab Emirates	679	401	664	1,048	1,277	533
Venezuela	5,093	4,548	5,374	5,942	7,529	3,221

Note: These claims were reported on the Country Exposure Report filed by banks on a consolidated basis comprising claims held by domestic offices, foreign branches, and majority-owned foreign subsidiaries.

Source: Federal Reserve System.