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THE ANNUAL MEETINGS OF THE INTERNATIONAL MONETARY FUND  
AND  
INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

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on Wednesday, September 30, 1964

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I am delighted to be back in San Francisco and to have the opportunity to meet with this distinguished group. For me, as for almost everyone else, San Francisco is a favorite city, and I always welcome the chance to visit here. On one of my first visits to San Francisco, I was collaborating on a research project with Eliot Swan and, from my long knowledge of his personal qualifications and professional abilities, I am very happy that he is now the President of the Federal Reserve Bank.

On my first visit out here, I encountered the famous Emperor Norton Treasure Hunt. As I recall, the first clue in the Chronicle was that the treasure was not buried under the Union Square Garage! To me there is some of the flavor of an Emperor Norton Treasure Hunt in much of the recent search for a pot of liquidity to solve the world's monetary problems. This is certainly true, for example, of the proposed creation of a new reserve asset composed partly of, and linked rigidly to, gold.

But not to get ahead of my story, I would like to talk with you today briefly about the annual meetings of the International Monetary Fund and International Bank for Reconstruction and Development held this year in Tokyo just three weeks ago.

As I view the meetings in the very short time there has been for any real perspective on them it seems to me that there were

three main threads or themes running through the conference, apart from the perennial question of increased capital for the less developed countries.

- 1) Increased international cooperation,
- 2) Increased flexibility of monetary institutions and arrangements,
- 3) Increased resources of the International Monetary Fund.

Prime Minister Ikeda of Japan sounded the keynote of increased international cooperation in his opening speech at the Annual Meetings, stressing "the fact that international financial cooperation has grown in substance and strength from year to year." And the tremendous postwar progress in Japan itself was attributed by the Prime Minister to the "climate of international cooperation which did not exist in former times". This theme was echoed by the General Chairman of the plenary sessions, Governor Francisco Aquino of El Salvador, who pointed out that "in Japan there is ample evidence of the benefits to be derived from dealing with economic problems through channels of international cooperation. Japan has received financial assistance from the Fund and the Bank. In other ways as well it has both benefited from and contributed to this process of international cooperation".

Similarly, there is ample evidence of the increased international cooperation that we in the United States, along with our European colleagues, have been experiencing, and benefiting from, during the past several years. In monthly meetings in Paris I have seen at first hand the development of a mutual understanding of the complex

problems facing each of the participating countries, an understanding that has provided a broader base for cooperative efforts. It would not be difficult to cite tangible results. A good example is the agreement among the so-called "Group of Ten"--the ten leading industrial countries--to participate in the General Arrangements to Borrow, which provides a sizeable addition to the resources of the International Monetary Fund, an addition designed to cope with any threatened impairment of the functioning of the international monetary system. Another case in point is the ad hoc, Basle type, arrangements in which central banks have provided assistance bilaterally to countries experiencing temporary speculative drains on their reserve positions. Our own network of Federal Reserve swap and stand-by swap arrangements, now totaling over \$2 billion, is another clear example of how we have benefited along with the other countries involved in the cooperative process of constructing this outer periphery of defenses for the dollar--defenses which also include the so-called "Roosa bonds", providing another medium for the investment of dollars acquired by surplus countries. And the most recent moves toward increased monetary tightness in European countries were tailored as far as practicable, at least, so as to avoid, or minimize, any possible disruptive external effects on other countries.

I speak with conviction on this matter of international cooperation because I believe that the very process of continuous confrontation--in Working Party 3 and the Economic Policy Committee of the OECD, in the G-10 Deputies and Ministers meetings, etc.--has been

one of the most useful and constructive recent achievements in the international monetary area. Simply to be able to sit down and talk directly and candidly with our financial official counterparts in the other leading countries is in itself, in my judgment, a great gain.

The second main theme of the Annual Meetings, that of increased flexibility of international monetary institutions and arrangements, again was highlighted by Governor Aquino in his opening remarks as the Chairman of the Boards of Governors of the several institutions. He paid glowing tribute to the Bretton Woods founders for providing both the Bank and Fund institutions with "not only a strong structural organization but also the necessary elasticity and flexibility to meet the changing economic problems of a changing world".

Significantly he then went on to point out that:

"I doubt that any one at Bretton Woods would have predicted that in 1964 each institution would have 102 member countries, or that we would meet here today as the Governors of not two, but four, great financial institutions. But these two facts testify how greatly the world has changed and how our institutions have had the flexibility to change with it."

Throughout his remarks Governor Aquino consistently stressed the flexibility and adaptability of the Bank and Fund organizations and of how institutional arrangements have been changed and adapted to changing needs. Again, it has been my privilege to witness this flexibility and adaptability in international monetary institutions and arrangements in action. The Bank's consortium device and the Fund's compensatory financing facilities are cases in point. And

I have already mentioned the bilateral and multilateral credit facilities developed in recent years which have greatly strengthened the workings of the international monetary system.

The focal point of this year's Bank and Fund meetings, however, and the third and really major theme of the conference, was the case for an increase in Fund quotas, a principal finding both of the Group of 10 Report issued August 10, 1964, and of the parallel Fund study on international liquidity included in its 19th Annual Report published on the same date. The Annual Meetings really centered on these reports and, more specifically, on the implementation of, and implications of, the key recommendation of the Group of Ten report calling for a moderate over-all general increase in Fund quotas, plus selective increases for those countries whose quotas are clearly out of line.

For perspective it is necessary to go back to the Annual Meetings held in Washington last year. At last year's meetings the Ministers and Governors of the Group of Ten initiated a study by their Deputies of the functioning of the international monetary system and its probable future needs for liquidity. The study was undertaken largely at the initiative of the United States, which recognized that in the long run the contribution of additional dollars to world reserves would not continue as in the past and also felt that it was most appropriate for representatives of leading countries, representing a substantial share of the resources of the International Monetary Fund, to search for principles that would be relevant to

the quinquennial review of Fund quotas already scheduled under the Fund's Articles of Agreement. At the meetings last year the International Monetary Fund itself also decided to have a similar and parallel study conducted by its staff. The two studies were carried out in close consultation since the ten countries are, after all, members of the Fund, and an official of the Fund participated in the meetings of the Deputies and Ministers of the Group of Ten.

The frame of reference for the Group of Ten study was contained in the Ministers and Governors Communique of October 2, 1963, in the following terms:

"In reviewing the longer-run prospects, the Ministers and Governors agreed that the underlying structure of the present monetary system--based on fixed exchange rates and the established price of gold--has proven its value as the foundation for present and future arrangements. It appeared to them, however, to be useful to undertake a thorough examination of the outlook for the functioning of the international monetary system and of its probable future needs for liquidity. This examination should be made with particular emphasis on the possible magnitude and nature of the future needs for reserves and for supplementary credit facilities which may arise within the framework of national economic policies effectively aiming at the objectives mentioned in paragraph 2 /high levels of economic activity, economic growth, price stability/. The studies should also appraise and evaluate various possibilities for covering such needs."

Implementing this, the Deputies of the Ten Group--including both a Treasury official and Central Bank representative. from most of the countries participating--met monthly, generally in Paris, with their efforts culminating in the Statement by the Ministers, and the accompanying Annex summarizing the results of the Deputies studies, on August 10, 1964--simultaneously with the release of

the Fund's Annual Report in which two chapters also deal with the question of international liquidity.

The principal conclusions and recommendations of the G-10 Statement and Annex were central to many of the addresses and much of the discussion at the Tokyo Bank-Fund Meetings. In brief, there were two principal conclusions and four recommendations in the G-10 report.

As to the conclusions, both Deputies and Ministers concluded that the present international currency system was functioning well, and reaffirmed that its underpinnings, in terms of fixed exchange rates and the established price of gold, had proven their continuing value as a foundation of the international monetary system. With an increase in Fund resources in prospect, they also concluded that liquidity was fully adequate for the present, so that any liquidity problem was one of the future, not a present problem.

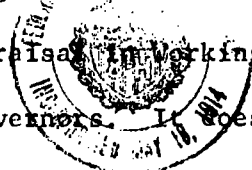
The G-10 recommendations were fourfold:

First, they recognized the close interrelationship between the need for liquidity and the speed and efficiency of the process of adjusting imbalances, noting that any step taken by one country to correct its balance of payments deficit or surplus is of concern to all, and affects total needs for liquidity. Accordingly, they recommended that Working Party-3 of OECD undertake a study of the adjustment process of correcting imbalances in international payments positions, with a view to determining appropriate policies for avoiding



or minimizing such imbalances. In assigning this task to Working Party-3 the intent was clearly not to have an abstruse academic analysis of the adjustment process, but rather to take advantage of the involvement of Working Party-3 in the day-to-day appraisal of what is currently happening--the events that typify the way in which the adjustment process is actually working--to test out the possibility of determining criteria or standards of adjustment.

Second, both the Deputies and the Ministers called for "multilateral surveillance of bilateral financing and liquidity creation"--basically nothing more nor less than a decision among the Ten to exchange information more promptly and regularly regarding means of financing any surpluses or deficits. As Chancellor Maudling pointed out at the Bank-Fund meetings this is "intended to represent a step forward along the road of increasing consultation and cooperation in monetary and economic affairs which we have been following ever since the end of the war". From the United States' standpoint, too, this process represents a formalizing and strengthening of existing international cooperation, particularly with respect to reporting arrangements. It will permit more informed, and useful, appraisal in Working Party-3 and among the central bank Governors. It does not, as Chancellor



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Maudling pointed out, "give any member of the Group of Ten, or indeed the Group as such, a veto on the setting up of new facilities within the Group or between members of it, or on the use of existing facilities. It does, however, recognize very clearly that arrangements made between individual countries may well be of close interest to other members of the Group, and that the interest of these other members should be taken fully into account when new arrangements are made".

The third major recommendation of the Group of Ten report was the formation of a so-called "Study Group on Creation of Reserve Assets". The assignment of this group looks to the future and to the possible problems of liquidity adequacy that might arise in the years ahead. This group is scheduled to examine various proposals regarding the possible creation of reserve assets either through the IMF or otherwise. The "otherwise" clearly refers to the views sketched by French Finance Minister Valery d'Estaing in his remarks at the Bank-Fund meetings calling for the creation of a collective reserve unit. The establishment of the study group reflects one important difference of emphasis in the G-10 and Bank-Fund discussions, namely, as to whether or not the principal concern, looking ahead, should be with finding a new means for creating owned reserves (over

and above gold and reserve currencies) or with enlarging and making more effective the credit facilities component of liquidity.

Finally, as I have indicated, the fourth recommendation in the Group of Ten report called for a moderate, general increase in Fund quotas, supplemented by selective increases for those countries whose quotas are clearly out of line.

Looking more closely at the Bank-Fund meetings in Tokyo against the background of the Group of Ten report of August, there was universal support for a general increase in quotas, with some expressing the view that it should be limited to 25% and others obviously feeling that a larger percentage would be more acceptable. The general move toward a quota increase began with a clear call by IMF Managing Director Schweitzer for an increase, followed by Secretary Dillon's supporting statement--the latter intended to be a statement of basic position which would prepare the way for action in the Fund next year. The call for quota increases met with support from many of the other Governors in their prepared statements, and culminated in the adoption by the Fund Governors of a draft resolution to the effect:

"That the Executive Directors proceed to consider the question of adjusting the quotas of members of the Fund and at an early date submit an appropriate proposal to the Board of Governors."

One important unresolved question related to the proposed quota increases is that of the gold payments (normally 25% of the quota

increase) to accompany such increases in subscriptions and the resultant possible impact of such gold payments on reserve currency countries, and on aggregate world reserves. With trade and payments expanding more rapidly than the supply of monetary gold, it is especially important that there be economy in its use. Since the United States is the only country maintaining gold convertibility--the foundation of the present system--it is especially significant that the Group of Ten and Fund reports called attention to the need for looking at methods of minimizing the impact, particularly on the reserve currency countries, of transfers to the Fund of gold from national reserves.

There are several ways in which this impact might be mitigated. Secretary Dillon clearly indicated that he regarded the French Finance Minister's suggestion of simply spreading out the quota contribution over two years or so an inadequate solution. An important part of any mitigation should, of course, be the payment of their gold subscriptions by principal countries, certainly those which have been accumulating gold in recent years, out of their own present holdings. In addition, there are a number of possibilities indicated in the Fund's Annual Report which would involve the Fund shifting some of the gold back, e.g., either by deposit or investment. Another answer, and perhaps the best answer, is to have at least part of the gold payment in gold certificates--in essence representing subscribed but uncalled gold.

An item of considerable interest in the meetings and corridor conversations was the statement by French Finance Minister d'Estaing

which sketched out some of the French differences of view regarding the future course of the payments system. Minister d'Estaing argued against the provision of liquidity via reserve currencies or additional "conditional liquidity" and called for the construction of a new collective reserve unit, rigidly tied to gold. This collective reserve unit would initially be created by a small group of countries. In one version it would represent the contribution by each of the countries of certain agreed amounts of their currencies to be put in a pot of currencies held in escrow by an agent (possibly the BIS) who, in turn, would issue claims in proportion to each country's contribution. Once created and issued the holdings of collective reserve units would bear a fixed relation to the gold held by each of the participating countries, and transfers would be in the same ratio of gold to CRUs as the prevailing ratio of total gold holdings of all participating countries to total CRUs created. (For example, if with \$30 billion of total gold holdings \$5 billion of CRUs were to be created, net settlement would require payment of one CRU and six units in gold.) Finally, the quantity of CRUs would be changed by an agreed voting system, probably initially once a year.

The United States' position with respect to the French proposal was clearly outlined by Secretary Dillon. Basically, he stated the following four objections:

- 1) The United States believes in a "multilateral framework" for handling problems of world liquidity, whereas the French arrangement would be confined to a small group of countries, possibly ten or less.

2) The French proposal, with a fixed link to gold, would be restrictive, and perhaps even contractive in the first instance, rather than flexibly adaptable to meet expanding needs.

3) The French diagnosis as to what may, or may not, be wrong with the present system is incorrect. Specifically, Secretary Dillon refused to accept the French view that the United States is to blame for the inflationary problem in Europe, noting that the European countries could readily solve this problem by a change in their restrictive trade policies, and a more liberal attitude toward the exporting of capital.

4) The United States believes in building on, rather than discarding, the present system. This, too, was stressed in the Fund's Annual Report and by both Managing Director Schweitzer and Chancellor Maudling in their prepared remarks at the Fund meetings.

Finally, of course, there is the fundamental question of whether what may be needed in the future is an additional reservoir of owned reserves created to meet supposed global needs which is the essence of the French proposal, or whether the real need in the future may not be, as it is currently, for an expansion of credit facilities in response to specific balance of payments requirements, and a greater recognition of the potentialities of the Fund. Even if an expansion of owned reserves in the future becomes

necessary it can be done within the Fund framework. The so-called "gold tranche" positions of member countries, representing drawing rights acquired by a country either as a result of previous gold payments to the Fund or of the use of its currency in loans to other countries, are useable on a virtually automatic basis and come very close to "owned reserves". In the United States we financed a large part of our deficit in 1961 and 1963 out of just such claims.

The preceding remarks have represented an effort to capture and capsule some of the flavor and substance of the Bank-Fund meetings. Clearly the subject of international liquidity will continue to receive much attention and study both in and outside the international monetary organizations. From these studies and the cooperative efforts among the countries involved I can only conclude, as did the Managing Director of the Fund, that "the international monetary system will emerge strengthened and even better equipped to serve the interests of the community of nations".