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Statement of

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Member, Board of Governors of the Federal Reserve System

before the

Committee on Foreign Relations

United States Senate

on

S. 3423
To Provide for United States Participation in the Facility Based on Special Drawing Rights in the International Monetary Fund

May 13, 1968

The Board of Governors of the Federal Reserve System supports the proposed Amendment to the IMF Articles of Agreement, and the legislation which is being put forward to bring about U.S. ratification of the Amendment to provide for establishment of the Special Drawing Rights facility. The Board believes that establishment of this facility will be very much in the interests of the United States.

Establishment of the system of Special Drawing Rights in the International Monetary Fund will mean that the growth of international monetary reserves will for the first time be subject to rational international decision. The need for establishing such a system arises from vital interests in maximum employment, production, and trade. All countries want their reserves to grow over time, with the growth of international trade and payments, but the supply of existing kinds of reserve assets, including gold, clearly will not be enough to meet this need. Unless world reserves grow at an adequate rate, some countries could gain reserves only at the expense of the reserve holdings of other countries. In an effort to avoid reserve losses, and, if possible, to achieve reserve gains, more and more countries would tend to adopt much more restrictive economic policies than they would otherwise be likely to follow. I need not spell out the vicious circle of world-wide deflation that general pursuit of such policies could produce. This is what makes Special Drawing Rights important to every worker, every businessman, every industrialist, and every banker in the country.

In stressing the tremendous value that this new system can have--for the world at large as well as for the United States--I do not want to exaggerate its probable impact in the years immediately ahead. We do not know when the SDR system will be activated, or at what rate the participating countries will agree to create SDR's in the first years. The growth of reserves could be too slow for some years to come. The only thing we can be sure about is that with the SDR facility in existence, reserve growth at an adequate rate will be possible; without that facility, the world economic outlook for the medium and longer term would be much less favorable.

I should like now to say something about the relation between SDR's and the March 17 decision by the member countries of the now-defunct gold pool to establish a two-market system for gold. As you know, the negotiations looking to the establishment of an SDR system were going on long before the mid-March meeting, held here in Washington, on the gold problem. In fact, most of the basic principles of the SDR system were agreed upon last September at Rio. It was this fact, as much as anything else, that made the two-market decision possible.

As stated in the Washington Communiqué of March 17, the central-bank Governors of the gold-pool countries concluded that "as the existing stock of monetary gold is sufficient in view of the prospective establishment of the facility for Special Drawing

Rights, they no longer feel it necessary to buy gold from the market." Since it is therefore essential that increases in world reserves of other types take place, SDR's should be available to serve that purpose.

In other words, while the prospective establishment of the SDR facility was a key factor making the two-market system possible, the fact that the two-market system was adopted reinforces the need to establish the SDR facility. If the SDR system were not to be established, the viability of the two-market system for gold would be seriously compromised.

For the reasons I have indicated, the Federal Reserve warmly supports the proposed Amendment of the IMF Articles of Agreement, and the legislation which is being put forward to provide for its ratification by the United States.