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From J. Tobin

Tobin Memo

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A Gold Agreement Proposal

1. The Problem

The gold problem is that foreign central banks hold $10.3 billion in dollars which can, at their discretion, be turned in to the U. S. Treasury for gold. These dollars are only one step removed from our gold stock. Removed only one step more are $8.6 billion of foreign private holdings of dollars, which can be sold to foreign central banks for their currencies. Finally, both these stocks of potential claims on U. S. gold can be augmented by further U. S. balance of payments deficits or by disbursements of international organizations holding dollars.

Foreign central banks vary widely in their practice and tradition regarding the shares of gold and dollars in their international reserves. Some, like the U.K., Switzerland, Holland, and Belgium, hold a high proportion of their reserves as gold. Others, like Germany, Japan, and Sweden, hold a substantial share of their reserves in dollars. This variation is a threat to the U. S. gold stock in two related respects. First, a shift of funds from a high-gold-ratio country to a low-gold-ratio country drains away U. S. gold. Second, the example of the others puts continuing pressure on the low-gold ratio countries to raise the gold proportion of their own reserves.

2. The Direct Solution

The direct solution is to obtain an agreement of the important countries to maintain the gold proportion of their reserves at or below a prescribed ratio. The effects of such an agreement would be:

(a) to immobilize outstanding official dollar holdings, removing them as a threat to the U. S. gold stock;

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(b) to limit the impact on U. S. gold stocks of future acquisitions of dollars by foreign central banks, either from present private holdings or from future U. S. deficits, to a prescribed fraction of such acquisitions.

In return for these substantial advantages the United States would have to:

(a) extend our current policy of holding foreign currency as a part of our reserves to the point that our ratio of gold to total reserves is governed by the same rules to which the other countries agree;

(b) guarantee the official dollar holdings against devaluation, in conjunction with a similar guarantee by other countries of our reserves held in their currencies.

An agreement of this kind would have great advantages to both sides. For the United States, it would substantially remove the dangers of a run on gold. It would not eliminate the necessity of correcting our balance of payments, but it would permit us to do so in deliberate and orderly ways which do not imperil our domestic economic growth, our foreign commitments, or world trade and prosperity. For our European creditors, the agreement would eliminate the unequally distributed risks they now attach to holding dollars and introduce real reciprocity in the treatment of their currencies. For all parties, it would provide stability in the international monetary environment.

The United States would have to repeal the 25 percent gold cover requirement on the Federal Reserve, or revise it to permit other forms

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