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THE U.S. BALANCE OF PAYMENTS
SECOND QUARTER 1970

Based on preliminary data, both customary indicators of change in the external position of the United States showed somewhat improved but still large deficits in the second quarter, the Commerce Department's Office of Business Economics announced today. The U.S. balance of payments on the liquidity basis, seasonally adjusted, was in deficit by $1,287 million, or $1,504 million excluding allocations of SDR. In either case, this represented a favorable shift of $263 million from the comparable figures for the first quarter of 1970. However, the improvement was more than accounted for by a large swing in special financial transactions.

The balance on the official reserve transactions basis, seasonally adjusted, was in deficit by $1,761 million in the second quarter ($1,978 million excluding allocations of SDR). This was an improvement of $1.1 billion from the record first quarter deficit. Fragmentary information suggests that part of the improvement was associated with shifts of funds by foreign official agencies from U.S. banks to the Eurodollar market. Such shifts improve the official balance but imply no genuine improvement in the external position of the United States. Large flows of volatile funds into Canada before the Canadian dollar appreciated and into Germany where monetary conditions were extremely tight contributed to the deficit.

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The liquidity balance

The liquidity balance is intended to be a broad indicator of potential pressures on the dollar resulting from changes in our liquidity position, and is measured by changes in U.S. official reserve assets and in liquid liabilities to all foreigners. However, this measure has been distorted in recent years by two factors, neither of which represents a change in our underlying position. The distorting factors are: 1) special financial transactions--mostly shifts of funds held by foreign official agencies and by international and regional organizations between liquid and nonliquid categories--and 2) flows of U.S. funds (mostly unrecorded) to the Eurodollar market which were returned to the United States through the foreign branches of U.S. banks.

Special financial transactions favorably affected the second quarter liquidity balance by $695 million--largely due to transactions totaling $800million by Canadian authorities--compared with an adverse impact of $254 million in the first. In the absence of this shift, the liquidity balance would have shown a $686 million deterioration from the first quarter to the second. With only partial data now available, it is not clear whether the liquidity deficit was significantly enlarged by outflows of U.S. funds to the Eurodollar market in the second quarter. Although the $574 million increase in the residual item--representing the balance of transactions for which data are not yet available--suggests the possibility of such outflows, the increase may have been due to other factors.

In addition to the $949 million swing in special financial transactions, the major factors contributing favorably to the $263 million improvement in the second quarter liquidity deficit were: 1) a $330 million increase in the merchandise trade surplus, as exports rose strongly and imports moderately; 2) a $178 million decline in net purchases of foreign securities by U.S. residents, as new Canadian issues dropped sharply; 3) a small increase in foreign purchases of U.S. securities (other than Treasury issues), as a rise in new Eurobonds was only partly offset by a drop in foreign purchases of outstanding U.S. bonds and by a small increase in net foreign sales of U.S. stocks.

These favorable shifts totaled almost $1.5 billion. The major adverse shift, in addition to the $574 million increase in the residual item, was a $656 million swing in bank reported claims, largely reflecting outflows of funds not covered by the Foreign Credit Restraint Program to Canada and Japan.

The "official" balance

The official reserve transactions balance is intended to be an indicator of immediate exchange market pressures on the dollar during the reporting period. In addition to changes in U.S. official reserve assets,

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it takes account of changes in liabilities only to foreign official agencies, but includes changes in both liquid and certain nonliquid liabilities. This measure of actual market pressure has also been distorted occasionally. Fragmentary information suggests that in the second quarter shifts to the Eurodollar market of funds previously held by foreign official agencies in U.S. banks tended to reduce the size of the official deficit. Such shifts indicate neither a strengthening of the dollar in the exchange market nor a loss of dollars by foreign official agencies.

The major item accounting for the larger improvement in the official balance than in the liquidity balance in the second quarter was a $1.8 billion favorable swing in the flow of foreign private liquid funds.[1] In the first quarter--when there was a sharp easing in monetary conditions in the United States and in the Eurodollar market--both U.S. banks' liabilities to their foreign branches and liquid liabilities to other private foreigners showed a sharp drop, with total outflows of foreign private liquid funds of over $1.7 billion. In the second quarter there was a small inflow of such funds (as U.S. banks' liabilities to their branches showed a small increase). Aside from the shift of funds by foreign official agencies from U.S. banks to the Eurodollar market, the improvement in this flow may have been associated with the temporary tightening in U.S. and Eurodollar monetary conditions, which encouraged private foreigners to hold dollars. In addition, U.S. banks may have been discouraged from further reductions in liabilities to their branches as such liabilities approached their historical base levels; the base for individual banks is reduced if liabilities go below it, and later increases in liabilities would become subject to reserve requirements.

On the other hand, the inflow of foreign private liquid funds in the second quarter might well have been larger had it not been for anticipations that the Canadian dollar would increase in value (it was permitted to float upward beginning May 31) and the sharp tightening of monetary policy in Germany. As a result there were very large inflows of funds into both Canadian dollars and German marks. France also continued to make dollar gains, but the inflow into the United Kingdom fell off from the extraordinary inflow in the first quarter.

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1. After adjusting the recorded liquidity balance for changes in certain nonliquid liabilities to foreign official agencies, which affect the liquidity balance but not the official balance, the adjusted liquidity balance shows a deterioration of almost $0.7 billion in the second quarter. The difference between that deterioration and the $1.1 billion improvement in the official balance is fully explained by the $1.8 billion favorable shift in foreign liquid private funds.

Financing the Balances

U.S. official reserve assets decreased $1,022 million in the second quarter. (Figures in this section are not seasonally adjusted.) The decline reflected: 1) a decrease of $14 million in official gold holdings; 2) an increase of $37 million in SDR; 3) a decrease of $818 million in U.S. official holdings of convertible foreign currencies, as net repayments by foreigners of drawings on mutual swap facilities with the United States continued for the third successive quarter; and 4) a decrease of $227 million in our gold tranche position--essentially, our automatic drawing rights--at the IMF, reflecting a $150 million drawing by the United States and $77 million in net repayments by foreigners of U.S. dollars to the IMF.

Liquid liabilities to all foreigners increased $475 million. This increase, plus the $1,022 million decrease in reserve assets, equaled the liquidity deficit of $1,497 million. Liquid liabilities to foreign commercial banks decreased $72 million, with only a small rise in U.S. banks' liabilities to their foreign branches. Liquid liabilities to foreign official agencies increased $528 million; those to international and regional organizations declined $123 million; and those to other foreigners rose $142 million.

The second quarter deficit of $2,063 million on the official reserve transactions basis consisted of the $528 million increase in liquid liabilities to foreign official agencies, a $513 million rise in certain nonliquid liabilities to them, and the $1,022 million decrease in U.S. reserve assets.

Further Details of Major Transactions

Special financial transactions

Special financial transactions, seasonally adjusted, improved the liquidity balance by $695 million in the second quarter, compared with an adverse impact of $254 million in the first. Most of the $949 million favorable shift reflected transactions also classified as "certain nonliquid liabilities" to foreign official agencies, which increased $506 million in the second quarter after declining $422 million in the first. Other special financial transactions favorably affected the balance by $189 million, as compared with $168 million in the first.

The principal favorable transaction in the second quarter was the $800 million purchase by Canada of nonmarketable, medium-term U.S. Government securities; Canada made $300 million of such purchases in the first quarter. Transactions under agreements to offset U.S. military expenditures in Germany favorably affected the liquidity balance by $186 million;

in the first quarter, Germany had liquidated $542 million of nonmarketable, medium-term U.S. Government securities previously purchased. Other favorable transactions in the second quarter were $94 million in purchases of agency bonds by international and regional organizations and $15 million of nonscheduled repayments of U.S. Government credits (including sales of foreign obligations to foreigners) other than those to Germany under the offset agreements.

Partly offsetting the favorable transactions were a $89 million liquidation of nonconvertible U.S. Treasury securities issued to Italy in connection with military purchases in the United States; a $230 million reduction in long-term liabilities to foreign official agencies; and a $48 million reduction in long-term liabilities to international and regional organizations.

The balance measured on the official reserve transactions basis is affected neither by shifts between liquid and certain nonliquid liabilities to foreign official agencies nor by similar shifts in liabilities to international and regional organizations. The remaining special financial transactions favorably affected the official reserve transactions balance by $143 million in the second quarter, as compared with $73 million favorable impact in the first.

Merchandise trade

The balance on merchandise trade reached a surplus of $848 million, seasonally adjusted, in the second quarter, with exports of $10,706 million and imports of $9,858 million. This represented a $330 million increase in the surplus, much larger than the $70 million gain in the first quarter and the $130 million gain in the fourth. For the first half of 1970, the surplus was at an annual rate of $2.7 billion, compared with a surplus of only $0.6 billion for the full year 1969, when the impact of the dock strike produced trade deficits during the first half of the year. (These figures are on a balance of payments basis which excludes "military" exports and imports and reflects various other adjustments to the trade data reported by the Census Bureau.)

The $330 million improvement in the second quarter surplus largely reflected a $465 million rise in exports, $60 million more than in the first quarter, as economic activity abroad continued strong. Imports advanced only $135 million, $200 million less than in the first quarter, suggesting that the earlier slowdown in the domestic economy might be having some effect.

While most of the $465 million increase in second quarter exports was in nonagricultural goods, agricultural shipments scored an unexpected $100 million gain, as exports of tobacco and grains recovered sharply. Agricultural exports had shown no advance in the preceding quarter from the high levels reached in the last quarter of 1969. The $365 million second quarter gain in nonagricultural exports was about $40 million below the first quarter rise. Exports of industrial supplies rose $125 million, including further large increases in iron and steel and in coal exports to Japan. This gain was nearly $100 million less than in the first quarter, as a $85 million increase in chemical exports was not repeated. Machinery exports rose $100 million, about the same as in the first quarter. Exports of civilian aircraft rose barely $20 million, after increasing $160 million in the first. Stepped-up deliveries of the new jumbo jets were nearly offset by declines in conventional transport planes which had been surprisingly strong in the first quarter. In contrast, automotive exports, principally passenger cars to Canada, rose $140 million, compared with a $40 million drop in the first quarter. Exports of nonfood consumer goods and other commodities showed only minor changes.

The modest $135 million increase in imports was $200 million smaller than the first quarter rise. Although special factors were partly responsible for this deceleration, the slowdown in the U.S. economy may also have had some influence. Nonfood consumer goods rose only $25 million in the second quarter, compared with $200 million in the first. Industrial supplies and materials fell by nearly $100 million, following a $70 million rise. About half of the second quarter drop was in petroleum, which may have been affected by special factors such as recent increases in tanker rates and the full effect of mandatory quotas imposed earlier on Canadian oil imports. Machinery imports remained unchanged, after rising $60 million in the first quarter.

Partly offsetting these downward shifts was an unusual $210 million rise in second quarter automotive imports, which followed a $140 million fall. The increase was shared about equally between U.S.-affiliated Canadian producers and overseas auto suppliers, while the entire first quarter drop was in imports from Canada. A large part of the second quarter gain can be attributed to the recovery in domestic demand for automobiles. Sales of both U.S.-type autos (such as are made in Canada) and foreign autos increased, with the share of foreign autos rising; this was accompanied by some rebuilding of dealers' inventories of U.S.-type cars following sizable liquidations in the first quarter.

Imports of foodstuffs rose about $50 million in the second quarter, compared with $120 million in the first when special factors were important. A recovery in coffee, with both volume and prices higher, was largely responsible for the second quarter gain. Meat imports, which had been inflated in the first quarter, declined to more normal levels.

Other categories of imports in the second quarter showed an accumulation of small declines.

Bank reported claims

Bank reported claims, seasonally adjusted, increased $486 million, after a decrease of $170 million in the first quarter. Long-term claims declined $46 million, following a $26 million decrease. In contrast, short-term claims rose $532 million in the second quarter after falling $144 million in the first. About three-quarters of this outflow was due to a rise in collections and acceptances. Japan accounted for almost $200 million of the increase, which was probably associated with the tight monetary conditions in that country and in Europe. There was also a $190 million increase in short-term claims on Canada, where monetary conditions remained relatively tight. More than half of the increase was in deposits and money market paper. Claims on Mexico, Spain and Korea also increased. Almost all of the outflow in the second quarter reflected transactions not subject to the Foreign Credit Restraint Program.

U.S. transactions in foreign securities

U.S. transactions in foreign securities resulted in net U.S. sales of $19 million, seasonally adjusted, a favorable shift of $180 million from net purchases of $159 million in the first quarter. Purchases of new issues fell to $91 million from $402 million in the first quarter, mostly reflecting a $260 million decline in new Canadian issues. Several issues in the United States planned by Canada were postponed as long-term interest rates rose. In addition, the World Bank, which was responsible for $48 million of new issues in the first quarter, was not in the market in the second. Partly offsetting the decline in new issues, U.S. residents made net purchases of $15 million of outstanding foreign securities, an adverse swing of $130 million from the unusual net sales of $116 million in the first quarter. Redemptions showed little change.

Foreign transactions in U.S. securities

Net foreign purchases of U.S. securities were $308 million, up slightly from first quarter purchases of $297 million. Net foreign sales of U.S. corporate stocks increased about $40 million to $126 million. There were small net purchases in both April and June. In May, when U.S. stock prices fell sharply, there were net sales of almost $200 million. On the other hand, foreign purchases of Eurobonds newly issued by U.S. corporations increased from $155 million in the first quarter to $306 million in the second. The bulk of the $150 million increase was due to larger borrowing (and repatriation of the proceeds) through U.S. companies' finance subsidiaries incorporated in the Netherlands Antilles. The high yields offered on Eurobonds, while stock prices were declining worldwide, encouraged foreign investment in these instruments. Partly offsetting this increased inflow, foreign purchases of outstanding U.S. bonds fell almost $100 million to $128 million. This included $94 million of investment by international and regional organizations in U.S. agency bonds (counted as special financial transactions) in both the first and second quarters.

Data for the balance of payments items now available on a preliminary basis are shown in the attached table. Complete balance of payments data for the second quarter and further analysis will be published in the September issue of the Survey of Current Business, the monthly magazine of the Office of Business Economics. The Survey is available from field offices of the Department of Commerce, or from the Superintendent of Documents, U.S. Government Printing Office, Washington, D. C., 20402, at an annual subscription price of $9, including weekly supplements; single copy, $1.

Selected data on foreign transactions of the United States in the second quarter of 1970
available as of the middle of August, 1970

(Millions of dollars)

Credits +; Debits -	1968	1969 Year	1969 I	1969 II	1969 III	1969 IV	1970 Ir	1970 IIp	Adjusted for seasonal variations 1969 I	1969 II	1969 III	1969 IV	1970 Ir	1970 IIp	Shift IQ-IIQ
1. Merchandise trade, excluding military; net exports (+)	624	638	105	133	-204	604	671	1,014	-104	-21	318	445	518	848	330
2. Exports	33,588	36,473	7,438	9,872	8,965	10,198	10,129	11,019	7,472	9,585	9,581	9,835	10,241	10,706	465
3. Imports	-32,964	-35,835	-7,333	-9,739	-9,169	-9,594	-9,458	-10,005	-7,576	-9,606	-9,263	-9,390	-9,723	-9,858	-135
4. U.S. Government cash receipts associated with military sales contracts	966	1,449	236	322	298	593	198	220	236	322	298	593	198	220	22
5. U.S. transactions in foreign securities, net; U.S. purchases (-).	-1,254	-1,494	-364	-499	-506	-125	-204	59	-319	-539	-567	-69	-159	19	178
6. Foreign securities newly issued in the United States	-1,703	-1,667	-560	-277	-515	-315	-416	-99	-546	-269	-571	-281	-402	-91	311
7. Redemptions	546	478	130	85	80	183	127	125	130	85	80	183	127	125	-2
8. Other transactions, net	-97	-305	66	-307	-71	7	85	33	97	-355	-76	29	116	-15	-131
9. Claims reported by U.S. banks, net; increase (-)	253	-541	210	-557	386	-580	315	-544	68	-502	229	-336	170	-486	-656
10. Long-term	358	330	133	31	131	35	26	46	133	31	131	35	26	46	20
11. Short-term	-105	-871	77	-588	255	-615	289	-590	-65	-533	98	-371	144	-532	-676
12. Nonscheduled repayments on U.S. Government credits and sales of foreign obligations to foreign residents	269	-87	44	34	-154	-11	88	115	44	34	-154	-11	88	115	27
13. Transactions in U.S. securities other than Treasury issues, net; foreign purchases (+)	4,389	3,112	1,388	365	396	963	297	308	1,388	365	396	963	297	308	11
14. Stocks, net	2,096	1,565	752	152	169	492	-85	-126	752	152	169	492	-85	-126	-41
15. Eurobonds, newly issued by U.S. corporations[1]	2,144	1,029	401	152	218	258	155	306	401	152	218	258	155	306	151
16. Other bonds, net	149	518	235	61	9	213	227	128	235	61	9	213	227	128	-99
17. Long-term liabilities reported by U.S. banks, net; increase (+)..	606	-676	-49	-174	-265	-188	-150	-215	-49	-174	-265	-188	-150	-215	-65
18. Nonmarketable, long-term liabilities of U.S. Government, not associated with specific transactions, net;[2] increase (+)	2,010	-41	95	-171	-115	150	-242	800	95	-171	-115	150	-242	800	1,042
19. Liquid liabilities to all foreigners other than official agencies, net;[3] increase (+)	3,810	8,933	3,024	4,653	1,423	-167	-1,562	-53	2,842	4,742	1,180	169	-1,742	32	1,774
20. Liquid liabilities to foreign official agencies, net;[3] increase(+)	-3,101	-525	-1,708	-538	2,235	-514	2,758	528)	-1,490	-941	1,099	-380	3,292	1,255	-2,037
21. U.S. official reserve assets, net; increase (-)	-880	-1,187	-48	-299	-686	-154	-386	1,022)							
22. Gold	1,173	-967	56	-317	-11	-695	-44	14							
23. SDR	-	-	-	-	-	-	-920	-37							
24. Convertible currencies	-1,183	814	-73	246	-442	1,083	831	818							
25. Gold tranche position in IMF	-870	-1,034	-31	-228	-233	-542	-253	227							
26. Allocations of special drawing rights (SDR)	-	-	-	-	-	-	867	-	-	-	-	-	217	217	-
27. Special financial transactions not included in lines 1-26, net;[4] favorable effect on liquidity balance (+)	-167	-53	-7	-1	-11	-34	-31	-84	-15	-8	-19	-11	-39	-91	-52
28. Other transactions (derived as residual)	-7,525	-9,528	-2,926	-3,268	-2,797	-537	-2,619	-3,170	-2,696	-3,107	-2,400	-1,325	-2,448	-3,022	-574
Memorandum items															
A. Special financial transactions, net;[4] favorable effect on liquidity balance (+)	2,723	-628	215	-367	-510	34	-246	702	207	-374	-518	57	-254	695	949
B. Balance on liquidity basis[5] including allocations of special drawing rights	171	-7,221	-1,268	-3,816	-2,972	835	-810	-1,497	-1,352	-3,801	-2,279	211	-1,550	-1,287	263
C. Balance on liquidity basis excluding allocations of special drawing rights	171	-7,221	-1,268	-3,816	-2,972	835	-1,677	-1,497	-1,352	-3,801	-2,279	211	-1,767	-1,504	263
D. Balance on official reserve transactions basis[6] including allocations of special drawing rights	1,641	2,708	1,711	1,204	-1,040	833	-1,958	-2,063	1,453	1,315	-582	522	-2,870	-1,761	1,109
E. Balance on official reserve transactions basis excluding allocations of special drawing rights	1,641	2,708	1,711	1,204	-1,040	833	-2,825	-2,063	1,453	1,315	-582	522	-3,087	-1,978	1,109

r. Revised. p. Preliminary
1. Excludes securities issued by U.S. subsidiaries incorporated abroad; however, if proceeds of such issues are transferred to U.S. parent companies they are treated as if they had been issued by U.S. corporations.
2. Includes medium-term securities and long-term obligations payable prior to maturity only under special conditions.
3. Liquid liabilities include foreign deposits in U.S. banks, private marketable debt obligations such as certificates of deposits and bankers acceptances, with an original maturity of less than one year, and marketable or convertible U.S. Government obligations. Government liabilities to foreign official organizations also include nonmarketable, convertible, medium-term U.S. Treasury securities and gold liabilities to the IMF. The distinction between liquid liabilities to foreign private and those to foreign official accounts is based on records of banks located in the United States. Liabilities to foreign private accounts include deposits of foreign branches of U.S. banks and of foreign commercial banks, associated with their U.S.-dollar denominated liabilities to foreign official agencies.
4. Special financial transactions are included in lines 6, 8, 12, 16, 17, 18, and 27. They reflect changes in near-liquid liabilities, nonscheduled repayments by foreign governments of U.S. credits, and other special financial transactions by U.S., foreign official, and international agencies.
5. Increase in U.S. official reserve assets and decrease in liquid liabilities to all foreigners (lines 19, 20, and 21 with sign reversed).
6. Increase in U.S. official reserve assets and decrease in liquid and certain nonliquid liabilities to foreign official agencies (lines 20 and 21, and parts of lines 17 and 18, and certain other nonliquid liabilities to foreign central banks and official agencies with sign reversed).

So[illegible] U.S. Department of Commerce, Office of Business Economics.